

SPENCER MUNICIPAL UTILITIES
INDEPENDENT AUDITORS' REPORTS
FINANCIAL STATEMENTS
AND SUPPLEMENTAL INFORMATION
DECEMBER 31, 2011 AND 2010

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SPENCER MUNICIPAL UTILITIES

OFFICIALS

<u>Board of Trustees</u>	<u>Title</u>	<u>Term Expires</u>
(Before July 2011)		
Dave Hultgren	Chairman	6-30-2011
Gary Tolzmann	Vice-Chairman	6-30-2012
Tom Howe	Secretary	6-30-2014
Murray Hart	Treasurer	6-30-2013
Sandi Schmidt	Trustee	6-30-2016
<u>Management</u>		
Steven Pick	General Manager	
Trisha Bruning	Finance Manager	
(After July 2011)		
Dave Hultgren	Chairman	6-30-2014
Gary Tolzmann	Vice-Chairman	6-30-2012
Sandi Schmidt	Secretary	6-30-2016
Murray Hart	Treasurer	6-30-2013
Alison Simpson	Trustee	6-30-2017
<u>Management</u>		
Steven Pick	General Manager	
Trisha Bruning	Finance Manager	

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SPENCER MUNICIPAL UTILITIES

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA**

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INDEPENDENT AUDITORS' REPORT

Board of Trustees
Spencer Municipal Utilities – Municipal Electric Utility
Spencer, IA 51301

We have audited the accompanying financial statements of The Municipal Electric Utility of the City of Spencer, Iowa (the Utility), as of and for the year ended December 31, 2011. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year comparative information has been derived from the Utility's 2010 financial statements and, in our report dated April 5, 2011, we expressed an unqualified opinion on the respective financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Utility as of December 31, 2011 and the respective changes in financial position and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 4, 2012, on our consideration of the Utility's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Funding Progress for the Retiree Health Plan information on pages 4 through 6 and page 26 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements taken as a whole. The supplementary information included on pages 27 through 29 is presented for purposes of additional analysis and is not a required part of the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Williams & Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 4, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS

The purpose of Management's Discussion and Analysis (MD&A) is to provide the reader with an introduction to the financial statements. Our discussion and analysis of the Municipal Electric Utility (Utility) of the City of Spencer, Iowa's financial performance provides an overview of the Utility's financial activities for the years ended December 31, 2011 and 2010.

The following information should be read in conjunction with the financial statements and the accompanying notes to the financial statements that follow this section.

2011 Financial Highlights

The Utility delivered approximately 165,800,000 kilowatt hours (kWh) of electricity to its retail customers in 2011 compared to approximately 155,700,000 kWh in 2010.

The Utility's net assets increased by \$233,201 to \$46,274,181 as a result of operations, a decrease in payables associated with Storefront Initiative and decrease in energy efficiency rebates paid to customers for the year ended December 31, 2011. The final year for the Storefront Initiative program was 2010. Over \$360,000 Storefront Initiative claims, payable to the City of Spencer, were submitted in December for payment at the January 2011 Board meeting.

Overview of the Financial Statements

The balance sheets include the Utility's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities).

The statement of revenues, expenses and changes in net assets report all revenues and expenses incurred during the fiscal year.

The Statement of Cash Flows present cash receipts, cash disbursements, and net changes in cash resulting from operations, capital and related financing activities and investing activities.

The notes to the financial statements provide the required disclosures and other information that is necessary to give the reader a complete understanding of the data provided in the statements. The notes present information about the Utility's accounting policies, material risks, obligations, commitments, contingencies and subsequent events.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Condensed Financial Information

The following condensed financial information serves as the key financial data and indicators for management, monitoring, and planning.

Condensed Balance Sheet

	<u>2011</u>	<u>2010</u>
Current assets	\$13,998,668	\$8,032,205
Noncurrent assets	6,719,013	10,454,385
Capital assets, net of depr.	38,973,465	37,285,463
Deferred costs	<u>203,761</u>	<u>94,220</u>
Total assets	<u>59,894,907</u>	<u>55,866,273</u>
Current liabilities	3,022,369	2,465,293
Bonds Payable	<u>10,598,357</u>	<u>7,360,000</u>
Total liabilities	<u>13,620,726</u>	<u>9,825,293</u>
Investments in capital assets, net of related debt	30,283,142	29,305,463
Restricted	2,081,214	2,419,391
Unrestricted	<u>13,909,825</u>	<u>14,316,126</u>
Total net assets	<u>46,274,181</u>	<u>46,040,980</u>
Total liabilities and net assets	<u>\$59,894,907</u>	<u>\$55,866,273</u>

Condensed Statement of Revenues, Expenses and Changes in Net Assets

Sales of electricity	\$10,208,176	\$9,247,080
Other	<u>1,332,181</u>	<u>1,035,733</u>
Total operating revenue	<u>11,540,357</u>	<u>10,282,813</u>
Power supply costs	7,498,554	7,294,083
Distribution system maintenance	1,541,041	1,622,168
Depreciation & amortization	2,468,227	2,437,741
Customer service & administration	<u>1,050,783</u>	<u>53,586</u>
Total operating expenses	<u>12,558,605</u>	<u>12,307,578</u>
Operating (loss)	(1,018,248)	(2,024,765)
Interest income	251,516	366,528
Interest expense	(340,271)	(360,351)
Other income	<u>1,340,204</u>	<u>543,139</u>
Total non-operating revenues	<u>1,251,449</u>	<u>549,316</u>
Change in net assets	233,201	(1,475,449)
Net assets, beginning of year	<u>46,040,980</u>	<u>47,516,429</u>
Net assets, end of year	<u>\$46,274,181</u>	<u>\$46,040,980</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS

Financial Analysis

The Utility's total assets increased by approximately \$4,029,000. This was primarily due to approximately \$3,040,000 from bond proceed deposited into a reserve for future improvements on the N4 scrubber project.

The Utility's gross revenues increased by approximately \$1,258,000 or 12.2% due to an approximate 10% electric rate increase for all usage effective 4/1/2011. In addition, kWh sales increased in 2011 compared to 2010 by approximately 10,000,000 kWh.

Total operating loss generated in 2011 was \$1,018,248 compared to an operating loss of \$2,024,765 in 2010.

Utility non-operating income (expense) resulted in \$1,251,449 of income, which was a 128% increase from 2010. This was due to a 58% decrease in Lieu of Property Taxes paid to the City of Spencer primarily affected by the completion of the Storefront Initiative project. In addition, the energy efficiency rebates decreased by approximately \$250,000 in 2011 compared to 2010.

Total net income (loss) increased from (\$1,475,449) in 2010 to \$233,201 in 2011.

Capital Assets and Debt Administration

Net capital assets increased by approximately \$1,688,000 due to assets placed in service exceeding depreciation.

Economic Factors

Retail sales increased by 4,400,000 kWh in 2011, Commercial sales increased by 3,300,000 kWh and Industrial sales increased by 1,300,000 kWh in 2011, which represents an approximate 7%, 4% and 18% increase, respectively, from 2010 to 2011.

The utility adopted an Energy Cost Adjustment (ECA) for all consumption beginning September 7, 2005. The ECA is calculated monthly and is designed to recoup the additional costs of power supply from the consumer.

Contacting the Utility's Financial Management

This financial report is designed to present our citizens, customers, and creditors with a general overview of the Utility's finances and operating activities. If you have any questions or require additional information please contact the Finance Manager, 712 Grand Ave, PO Box 222, Spencer, Iowa 51301.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF NET ASSETS
DECEMBER 31, 2011 AND 2010**

	2011	2010
ASSETS		
Current Assets:		
Cash and Cash Equivalents		
Unrestricted	\$ 1,600,674	\$ 828,811
Restricted	1,880,235	110,936
Board Designated	6,998,930	4,000,000
Consumer Deposits	76,895	74,711
Accounts Receivable (Net of Allowance for Doubtful Accounts of \$6,500 and \$5,600)	1,791,504	1,194,747
Unbilled Usage	225,770	470,381
Materials and Supplies Inventory	603,197	640,205
Fuel Inventory	469,565	376,898
Notes Receivable - City of Spencer	25,000	25,000
Prepayments	326,898	310,516
Total Current Assets	13,998,668	8,032,205
Capital Assets:		
Land	142,741	123,604
Construction in Progress	263,878	1,071,725
Plant in Service	76,800,103	72,044,438
Accumulated Depreciation	(38,233,257)	(35,954,304)
Total Capital Assets	38,973,465	37,285,463
Noncurrent Assets		
Noncurrent Investments:		
Unrestricted	326,706	-
Board Designated	1,501,070	4,500,000
Restricted	3,270,307	2,308,455
Notes Receivable - City of Spencer	620,930	645,930
Notes Receivable -Municipal Communications Utility	1,000,000	3,000,000
Unamortized Bond Issue Costs	203,761	94,220
Total Noncurrent Assets	6,922,774	10,548,605
Total Assets	\$ 59,894,907	\$ 55,866,273

See Accompanying Notes to Financial Statements

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF NET ASSETS
DECEMBER 31, 2011 AND 2010**

	2011	2010
LIABILITIES		
Current Liabilities:		
Accounts Payable	\$ 1,562,448	\$ 1,541,838
Payroll and Sales Tax Payable	34,994	31,623
Accrued Payroll and Compensated Absences	189,872	169,339
Accrued Interest Payable	24,460	27,782
Consumer Deposits	76,895	74,711
Deferred Revenue	3,700	-
Current Maturities of Long-Term Debt	1,130,000	620,000
Total Current Liabilities	3,022,369	2,465,293
Bonds Payable:		
Bonds Payable	11,728,357	7,980,000
Less - Current Maturities	(1,130,000)	(620,000)
Total Bonds Payable	10,598,357	7,360,000
Total Liabilities	13,620,726	9,825,293
NET ASSETS		
Net Assets		
Invested in Capital Assets, Net of Related Debt	30,283,142	29,305,463
Restricted	2,081,214	2,419,391
Unrestricted	13,909,825	14,316,126
Total Net Assets	\$ 46,274,181	\$ 46,040,980

See Accompanying Notes to Financial Statements

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**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	2011	2010
Operating Revenues:		
Residential	\$ 3,736,024	\$ 3,602,731
Commercial	4,834,447	4,402,309
Public Authorities	572,713	494,845
Sales for Resale	1,167,152	960,402
Energy Cost Adjustment Revenue	1,064,992	747,195
Penalties	22,212	20,281
Miscellaneous	142,817	55,050
Total Operating Revenues	11,540,357	10,282,813
Operating Expenses:		
Generation and Transmission		
Neal #4 Fuel and Generation	1,182,727	1,205,768
Walter Scott #4 Fuel and Generation	1,329,300	1,407,846
Purchased Power	4,871,318	4,586,423
Other	115,209	94,046
Distribution	1,541,041	1,622,168
Depreciation and Amortization	2,468,227	2,437,741
Customer Operations	345,750	348,432
General and Administrative	705,033	605,154
Total Operating Expenses	12,558,605	12,307,578
Operating (Loss)	(1,018,248)	(2,024,765)
Non-Operating Income (Expense):		
Interest Income on Investments	251,516	366,528
Resource Conservation	(230,339)	(483,166)
Economic Development Payment	(54,362)	(49,466)
Leased Facilities	2,082,204	2,143,817
Interest Expense	(340,271)	(360,351)
Gain (Loss) on Plant Retirements	18,780	(9,732)
Payment in Lieu of Property Taxes	(476,079)	(1,058,314)
Total Non-Operating Income (Expense)	1,251,449	549,316
Change in Net Assets	233,201	(1,475,449)
Net Assets at Beginning of Year	46,040,980	47,516,429
Net Assets at End of Year	\$ 46,274,181	\$ 46,040,980

See Accompanying Notes to Financial Statements

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	2011	2010
Cash Flows From Operating Activities:		
Cash Received From Customers	\$ 11,194,095	\$ 10,075,003
Cash Payments to Suppliers for Goods and Services	(8,243,468)	(7,434,958)
Cash Payments to Employees for Services	(1,874,437)	(1,834,594)
Cash Payments for Resource Conservation	(230,339)	(483,166)
Cash Payments for Economic Development and In Lieu of Property Taxes	(530,441)	(1,107,780)
Payments Received From Leasing of Facilities	2,082,204	2,143,817
Net Cash Provided By Operating Activities	2,397,614	1,358,322
Cash Flows From Capital and Related Financing Activities:		
Acquisition & Construction of Property and Equipment	(4,271,430)	(1,182,391)
Proceeds from Revenue Bond	8,973,554	-
Revenue Bond Principal Repayment	(5,225,000)	(595,000)
Proceeds from Sale of Capital Assets	22,125	-
Interest Paid	(343,593)	(362,447)
Net Cash (Used) By Capital and Related Financing Activities	(844,344)	(2,139,838)
Cash Flows From Investing Activities:		
Payments Received on Note Receivable -City of Spencer	25,000	609,331
Payments Received on Note Receivables - Communications	2,000,000	-
Proceeds From Redemption of Investments	3,750,000	5,775,000
Purchase of Investments	(2,037,510)	(1,775,000)
Interest Received From Investments	251,516	366,528
Net Cash Provided By Investing Activities	3,989,006	4,975,859
Net Increase in Cash	5,542,276	4,194,343
Cash and Cash Equivalents at Beginning of Year	5,014,458	820,115
Cash and Cash Equivalents at End of Year	\$ 10,556,734	\$ 5,014,458
Reconciliation:		
Cash and Cash Equivalents		
Unrestricted	\$ 1,600,674	\$ 828,811
Restricted	1,880,235	110,936
Board Designated	6,998,930	4,000,000
Consumer Deposits	76,895	74,711
	\$ 10,556,734	\$ 5,014,458

See Accompanying Notes to Financial Statements

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	2011	2010
Reconciliation of Operating (Loss) to Net Cash Provided by Operating Activities		
Operating (Loss)	\$ (1,018,248)	\$ (2,024,765)
Adjustments to Reconcile Operating (Loss) to Net Cash Provided By Operating Activities		
Depreciation and Amortization	2,468,227	2,437,741
Leased Facilities Income	2,082,204	2,143,817
Contributions Paid for Economic Development	(54,362)	(49,466)
Payment in Lieu of Property Taxes	(476,079)	(1,058,314)
Payment for Resource Conservation	(230,339)	(483,166)
(Increase) Decrease in Operating Assets:		
Accounts Receivable	(596,757)	(186,346)
Unbilled Usage	244,611	(37,139)
Materials and Supplies Inventory	37,008	38,902
Fuel Inventory	(92,667)	2,038
Prepayments	(16,382)	39,171
Increase (Decrease) in Operating Liabilities:		
Accounts Payable	20,610	494,068
Accrued Payroll and Compensated Absences	23,904	26,106
Consumer Deposits	2,184	15,675
Deferred Revenue	3,700	-
Total Adjustments	<u>3,415,862</u>	<u>3,383,087</u>
Net Cash Provided By Operating Activities	<u><u>\$ 2,397,614</u></u>	<u><u>\$ 1,358,322</u></u>

See Accompanying Notes to Financial Statements

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Basis of Accounting

The Municipal Electric Utility of the City of Spencer, Iowa (Electric Utility or Utility) operates as an independent unit of the City of Spencer and is managed, along with the Municipal Water Utility and the Municipal Communication Utility of the City of Spencer, Iowa, by a five member Board of Trustees.

The Utility follows the accounting practices prescribed through the Federal Energy Regulatory Commission for regulated utilities and proprietary fund accounting for governmental entities under accounting principles generally accepted in the United States of America.

For financial reporting purposes, the Utility has included all funds. The Utility has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Utility are such that exclusion would cause the Utility's financial statements to be misleading or incomplete. The Governmental Accounting Standards Boards has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Utility to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Utility. It was determined that the Utility has no component units.

The Utility is not considered to be a component unit of the City of Spencer for financial statement purposes.

The Utility's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when liability is incurred, regardless of the timing of related cash flows.

In reporting the financial activity of its enterprise fund, the Utility applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Boards Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure.

The Utility distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. The principal operating revenues of the Utility are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Capital Assets and Depreciation

Capital assets are stated at original cost when first devoted to public service. Currently, such costs include labor-related expenditures, such as payroll taxes, pensions, and other fringe benefits and administrative costs for labor related to the construction of new electric facilities. In addition, net interest costs on construction debt are capitalized. During 2011, the Utility did not have construction debt so no interest expense was capitalized.

Under a joint ownership agreement with other utilities, the Electric Utility has a 1.215% undivided interest in a 644 MW electric generation station known as George Neal Generating Station Unit No. 4. The Electric Utility's 1.215% ownership interest in this plant represents a total investment of \$5,221,156 included in utility plant in service with \$4,231,301 included in accumulated depreciation. Operating costs associated with this plant and depreciation are reflected in the statement of income.

Under a joint ownership agreement with other utilities, the Electric Utility has a 1.14% undivided interest in a 790 MW electric generation station known as Walter Scott, Jr. Energy Center Unit 4, which was placed in service in 2007. The Electric Utility's 1.07% ownership interest in this plant represents a total investment of \$15,905,363 included in utility plant in service with \$1,956,436 included in accumulated depreciation. Operating costs associated with this plant and depreciation are reflected in the statement of income.

Replacements and betterments of capital assets are charged to capital assets. Routine maintenance and repairs are charged to expense as incurred.

Depreciation is provided on a straight-line basis. Current depreciation expense is approximately 3.19% of the original cost of depreciable electric plant in service.

The estimated useful lives used to depreciate assets by class are as follows:

Infrastructure	20-33 years
Building and improvements	20 years
Equipment	5 years

C. Accounts Receivable

Accounts receivable are stated at the amount the Utility expects to collect from outstanding balances. The Utility provides for probable uncollectible amounts through a charge to earnings and a credit to valuation allowance based on its assessment the current status of individual accounts. Balances that are still outstanding after the Utility has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Inventories

Inventories are valued at the lower of cost or market. The average cost method is used for determining the cost of materials and supplies inventory. Inventories are recorded as an expenditure or, if applicable, capitalized when consumed.

E. Unamortized Bond Issue Costs

Unamortized debt issue costs are amortized over the life of the debt on a straight-line basis which approximates the effective interest method.

F. Net Assets

Net assets represent the difference between assets and liabilities in the financial statements. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used for acquisition, construction or improvement of those assets and increased by unspent proceeds. Net assets are reported as restricted when there are limitations imposed on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

G. Income Taxes

The Electric Utility is exempt from federal and state income taxes because it is a governmental entity organized under the provisions of Chapter 388 of the Code of Iowa.

H. Revenues and Unbilled Usage

Revenues are based on billing rates, which are applied to customers' consumption of electricity. The Utility records estimated unbilled revenue at the end of accounting periods. Revenues earned, but not yet billed at December 31, 2011 and 2010, totaled \$225,770 and \$470,381, respectively.

I. Estimates

The preparation of the financial statements in conformity in U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 2 - CASH AND CASH EQUIVALENTS AND NONCURRENT INVESTMENTS

The Utility's deposits in Banks at December 31, 2011 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Utility is authorized by statute and Board of Trustees' approval to invest public funds in obligations of the United States government, its agencies, and instrumentalities; certificates of deposit and other evidences of deposit at federally insured Iowa depository institutions; and the Iowa Public Agency Investment Trust.

The Utility had investments in Iowa Public Agency Investment Trust which are valued at an amortized cost of \$0 in pursuant to Rule 2a-7 under the Investment Company Act of 1940.

Interest Rate Risk – The Utility's investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days, but the maturities shall be consistent with the needs and use of the Utility.

Credit Risk – The Utility's investment in the Iowa Public Agency Investment Trust is unrated.

The Utility considers all highly liquid investments with an original maturity of three months or less to be cash equivalents for purposes of the statement of cash flows.

Investments are recorded at cost which approximates market. Adjustments are made to cost for any premium or discount, which is amortized over the maturity of the investment. Adjustments are also made to account for the change in accrued interest on respective investments.

Reconciliation of the Utility's cash and cash equivalents and noncurrent investments is as follows:

Cash and cash equivalents:	2011	2010
Board designated	\$ 6,998,930	\$ 4,000,000
Consumer Deposits	76,895	74,711
Restricted	1,880,235	110,936
Unrestricted	1,600,674	828,811
Total cash and cash equivalents	10,556,734	5,014,458
Noncurrent investments:		
Unrestricted	326,706	-
Board designated	1,501,070	4,500,000
Restricted	3,270,307	3,308,455
Total noncurrent investments	5,098,083	6,808,455
Total cash and cash equivalents and noncurrent investments	\$15,654,817	\$11,822,913

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 3 - BOARD DESIGNATED FUNDS

The Board of Trustees of the Utility has designated certain funds to be placed in a replacement and construction reserve account. These funds, which are from unrestricted net assets, are being designated for replacement of property, plant and equipment and for new construction. These funds cannot be expended without Board approval.

Assets of the funds as of December 31, 2011 are summarized as follows:

	Replacement and Construction Reserve
Cash and cash equivalents	\$ 6,998,930
Noncurrent investments	1,501,070
Total	<u>\$ 8,500,000</u>

Assets of the funds as of December 31, 2010 are summarized as follows:

	Replacement and Construction Reserve
Cash and cash equivalents	\$ 4,000,000
Noncurrent investments	4,500,000
Total	<u>\$ 8,500,000</u>

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 4 - CAPITAL ASSETS

Capital assets activity for the year ended December 31, 2011 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 123,604	\$ 19,137	\$ -	\$ 142,741
Construction in progress	1,071,725	864,104	(1,671,951)	263,878
Total capital assets not being depreciated	1,195,329	883,241	(1,671,951)	406,619
Capital assets being depreciated:				
Infrastructure	64,599,373	2,731,654	(23,730)	67,307,297
Buildings and improvements	728,875	1,561,837	-	2,290,712
Equipment	6,716,190	635,020	(149,116)	7,202,094
Total capital assets being depreciated	72,044,438	4,928,511	(172,846)	76,800,103
Less accumulated depreciation	35,954,304	2,453,406	(174,453)	38,233,257
Total capital assets being depreciated - net	36,090,134	2,475,105	1,607	38,578,846
Capital assets - net	\$37,285,463	\$3,358,346	\$(1,670,344)	\$38,973,465

Capital assets activity for the year ended December 31, 2010 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 86,092	\$ 37,512	\$ -	\$ 123,604
Construction in progress	554,345	584,216	(66,836)	1,071,725
Total capital assets not being depreciated	640,437	621,728	(66,836)	1,195,329
Capital assets being depreciated:				
Infrastructure	64,426,386	223,984	(50,997)	64,599,373
Buildings and improvements	706,775	22,100	-	728,875
Equipment	6,221,189	495,001	-	6,716,190
Total capital assets being depreciated	71,354,350	741,085	(50,997)	72,044,438
Less accumulated depreciation	33,572,633	2,423,956	(42,285)	35,954,304
Total capital assets being depreciated - net	37,781,717	(1,682,871)	(8,712)	36,090,134
Capital assets - net	\$38,422,154	\$(1,061,143)	\$(75,548)	\$37,285,463

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 5 - TRANSFERS IN LIEU OF PROPERTY TAXES/NOTE RECEIVABLE

By resolution of the Board of Trustees, voluntary transfers in lieu of property taxes are made to the City of Spencer, Iowa. Currently, transfers approximate 5% of gross sales (excluding the energy cost adjustment), less actual property taxes paid (on the George Neal Generating Station Unit No. 4 and on the Walter Scott Jr. Unit No. 4) and returned to the City of Spencer, Iowa. Additionally, funds declared to be surplus can be, and have been, transferred to the City.

During 2007, the Utility loaned the City \$375,000 to fund the economic development loan to Shine Bros. Corp. The City reimburses the Utility in equal payments of \$2,083 without interest, payable monthly. The balance of this note at December 31, 2011 was \$262,500 and December 31, 2010 was \$287,500.

A loan agreement was executed on June 1, 2009 between Spencer Municipal Utilities and the City of Spencer. The City has the ability to borrow up to \$1,000,000 at 2.75% until the maturity date of December 1, 2010, at which time all principal and interest is due. The loan was for the purpose of covering the cost to construct street and sewer improvements at the Green Industrial Center site. As of December 2010, the loan was paid in full which was comprised of a \$630,000 principal payment and \$20,220.41 in accrued interest.

A loan agreement was effective on July 15, 2009 between Spencer Municipal Utilities and the City of Spencer. The City borrowed \$383,430 for the purposes of loaning to Spencer Industries Foundation, Inc. The funds were used to construct an industrial building. The City is to repay the loan the earlier of the sale or lease of the building or by July 15, 2019. Interest will not accrue on the loan until July 15, 2014 at a rate of 3%.

Note 6 - NOTE RECEIVABLE – MUNICIPAL COMMUNICATIONS UTILITY

The Board of Trustees has approved an \$8,000,000 line of credit for the Municipal Communications Utility for use in start-up and construction costs related to bringing the Communications Utility into operation. The balance of the line of credit at December 31, 2011 and 2010 was \$1,000,000 and \$3,000,000, respectively. Outstanding balances bear interest at a rate of 4.5% per annum.

Note 7 – BONDS PAYABLE

Bonds payable activity for the year ended December 31, 2011 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Series 2004 revenue bonds	\$4,605,000	\$ -	\$4,605,000	\$ -	\$ -
Series 2008 revenue bonds	3,375,000	-	620,000	2,755,000	645,000
Series 2011 revenue bonds	-	8,950,000	-	8,950,000	485,000
Total revenue bonds	<u>\$7,980,000</u>	<u>\$8,950,000</u>	<u>\$5,225,000</u>	<u>\$ 11,705,000</u>	<u>\$1,130,000</u>

Bonds Payable listed on Statement of Net Assets include Unamortized Bond Premiums of \$23,357.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 7 – BONDS PAYABLE (Continued)

During 2011 the 2004 bonds were refinanced into the 2011 bonds to take advantage of low interest rates which resulted in a 1% rate reduction. The remaining \$4,345,000 was borrowed for purchasing additional ownership interest in WS4 as well as covering future construction costs in the N4 scrubber project.

The Series 2004, 2008 and 2011 revenue bonds require annual principal payments, due December 1, and semiannual interest payments, due June 1 and December 1. Interest rates throughout the term of the bonds range between 1.5% and 4.6 %. The bonds are secured by the future net revenues of the Utility. Long-term debt matures and bears interest as follows:

	Series 2008		Series 2011	
	Principal	Interest	Principal	Interest
2012	\$ 645,000	\$ 121,412	\$ 485,000	\$ 173,738
2013	670,000	94,000	495,000	166,463
2014	700,000	65,190	505,000	159,038
2015	740,000	34,040	505,000	151,463
2016	-	-	1,080,000	143,888
2017-2021	-	-	5,880,000	412,773
Total	\$ 2,755,000	\$ 314,642	\$ 8,950,000	\$ 1,207,363

The bond resolutions provide certain covenants relating to the collection, segregation, and distribution of revenues from customers; places certain restrictions on future borrowing and leasing or disposition of assets; and requires that minimum insurance coverage be maintained.

Revenue Bonds

The Utility has pledged future utility revenue, net of specified operating expenses, to repay outstanding utility revenue bonds. The bonds are payable solely from the utility's net revenues and are payable through 2021. The total principal and interest remaining to be paid on the bonds is \$13,135,818. Principal and interest due for the current year and total combined utilities net revenues were \$1,449,978 and \$955,240, respectively.

Restricted Funds

Outstanding Electric Revenue Bonds are collateralized by the revenue of the Utility and the various special funds established by bond covenants. The covenants provide that the revenue of the Utility is to be used first to pay operating and maintenance expenses of the system and second to establish and maintain the special funds. Remaining revenues may then be used for any lawful purpose. The covenants also contain provisions which, among other items, restrict the issuance of additional revenue bonds unless the special funds noted above contain the required amounts and certain financial ratios are met. As of December 31, 2011 the Utility is in compliance with all bond covenant requirements.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 7 – BONDS PAYABLE (Continued)

At December 31, 2011, the special funds consisted of the following:

	Cash and Cash Equivalents	Noncurrent Investments	Total
Bond Sinking Fund	\$ 125,617	\$ -	\$ 125,617
Bond Reserve Fund	-	1,232,813	1,232,813
Bond Improvement Fund	750,123	-	750,123
Total Restricted Net Assets	\$ 875,740	\$ 1,232,813	\$ 2,108,553

At December 31, 2010, the special funds consisted of the following:

	Cash and Cash Equivalents	Noncurrent Investments	Total
Bond Sinking Fund	\$ 79,642	\$ -	\$ 79,642
Bond Reserve Fund	-	1,558,039	1,558,039
Bond Improvement Fund	-	750,416	750,416
Total Restricted Net Assets	\$ 79,642	\$ 2,308,455	\$ 2,388,097

Monthly deposits into two bond sinking funds are required to establish the amount necessary to pay the next installments of principal and interest on the 2008 and 2011 Electric Revenue Bonds. Bond reserve funds for the 2008 and 2011 Electric Revenue Bonds equaled the required balance at December 31, 2011; therefore monthly deposits into the fund are not currently required. These funds may be used to pay principal and interest payments when insufficient funds are available in the sinking fund.

The bond improvement fund balance at December 31, 2011 equaled the minimum balance required; therefore monthly deposits into the fund are not currently required. These funds are to be used first for principal and interest payments when insufficient funds are available in the sinking and reserve funds and second for extraordinary unbudgeted maintenance expenses or system repairs, renewals and replacements.

Note 8 - RATE MATTERS

Rates of the Utility are established by the Board of Trustees and, as a municipal system, are not subject to the regulation of the Utilities Division of the Department of Commerce of the State of Iowa.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 9 - NUMBER OF METER CONNECTIONS

The number of meter connections totaled 6,084 at December 31, 2011 and 2010, respectively.

Note 10 - LEASES

The Utility leases electrical generation capacity of a jet turbine generator, its share of the Neal 4 plant, its share of the Wisdom 2 plant, and its share of the Walter Scott 4 plant under operating leases to other utilities or their associations. The revenues from such leases are classified as leased facilities. The Utility's investment in these facilities is included in capital assets in service and is set forth as follows:

	2011	2010
Jet turbine generator	\$ 2,537,488	\$ 2,537,488
Neal 4 plant	5,221,156	4,875,630
Wisdom 2 plant	2,314,530	2,314,530
Walter Scott 4 plant	15,905,363	14,666,778
Total	<u>25,978,537</u>	<u>24,394,426</u>
Less accumulated depreciation	<u>(8,925,807)</u>	<u>(8,240,619)</u>
Net investment	<u>\$17,052,730</u>	<u>\$ 16,153,807</u>

The lease of the Neal 4, Walter Scott 4 and Wisdom 2 plant are long-term commitments based on capacity. The amount is determined by formula based on usage and totaled \$4,266, \$1,007,160 and \$174,241, respectively, in 2011. The leases of the jet turbine generator are both by non-cancelable lease and a variable lease determined by capacity and totaled \$54,987 in 2011 and \$99,008 in 2010. The following is a schedule of future minimum rentals on non-cancelable operating leases on the jet turbine generator as of December 31, 2011:

2012	\$ 65,000
2013	65,000
2014	65,000
2015	120,000
2016	<u>120,000</u>
Total minimum lease payment receivable	<u>\$ 435,000</u>

The Utility leases bandwidth, property, and building space to the Water Utility and Communications Utility. The revenues from such leases are classified as leased facilities and

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 10 – LEASES (Continued)

totaled \$436,391 and \$432,871 in 2011 and 2010, respectively. The leases are 20-year variable leases based on bandwidth and space utilized. The payable at December 31, 2011 and 2010 was \$413,510 and \$413,511, respectively.

The Utility leases building space from the Water Utility. The expense from the lease is classified as operating expense. The lease is a monthly lease based on building space utilized and totaled \$9,600 in 2011 and 2010. The payable at December 31, 2011 and 2010 was \$9,600.

Note 11 - RETIREMENT SYSTEM

IPERS

The Utility contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, PO Box 9117, Des Moines, Iowa, 50306-9117.

Plan members were required to contribute 4.50% through June 30, 2011 and 5.38% presently of their annual salary and the Utility was required to contribute 6.95% through June 30, 2011 and 8.07% presently of annual payroll. Contribution requirements are established by State statute. The Utility's contributions to IPERS for the years ended December 31, 2011, 2010 and 2009 were \$132,694, \$118,799 and \$111,230, respectively, equal to the required contributions for the year.

Employees Pension Plan

All full-time employees of the Electric Utility who have completed six months of continuous employment and are 18 years of age are eligible to participate in a 457b Pension Plan administered by Security National Bank. The Utility contributes 8% of the employees' compensation for all employees contributing at least 2% of their salary.

The Electric Utility's contribution to the 457b Pension Plan for 2011 and 2010 totaled \$137,824 and \$138,560, respectively.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 12 – OTHER POST EMPLOYMENT BENEFITS

Plan Description. The Utility operates a single-employer retiree benefit plan which provides medical/prescription drug benefits for retirees and their family.

The medical/prescription drug coverage is provided through a fully-insured plan. Retirees under age 65 pay the same premium for the medical/prescription drug benefit as active employees, which results in an implicit subsidy and an OPEB liability.

Funding Policy. The Utility currently finances the retiree benefit plan on a pay-as-you-go basis.

Annual OPEB Cost and NET OPEB Obligation. The Utility's annual other post-employment benefit (OPEB) cost is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty years.

The following table shows the components of the Utility's annual OPEB for the year, the amount actually contributed to the plan, and changes in the Utility's net OPEB obligation to the plan:

	<u>2011</u>	<u>2010</u>
Annual required contribution	\$ 26,897	\$ 16,514
Interest on net OPEB obligation	1,198	774
Adjustment to annual required contribution	<u>(1,190)</u>	<u>(771)</u>
Annual OPEB cost (Expense)	26,905	16,517
Contributions made	<u>(14,928)</u>	<u>(5,939)</u>
Increase in net OPEB obligation	11,977	10,578
Net OPEB obligation – beginning of year	<u>29,948</u>	<u>19,370</u>
Net OPEB obligation – end of year	<u>\$ 41,925</u>	<u>\$ 29,948</u>

The Utility's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation were as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2011	\$ 26,905	55%	\$ 41,925
2010	\$ 16,517	36%	\$ 29,948

Funded Status and Funding Progress. The funded status of the plan as of December 31, 2011 was as follows:

	<u>2011</u>	<u>2010</u>
Actuarial accrued liability (AAL)	\$ 320,816	\$ 160,019
Actuarial value of plan assets	<u>-</u>	<u>-</u>
Unfunded actuarial accrued liability (UAAL)	<u>\$ 320,816</u>	<u>\$ 160,019</u>
Covered payroll (active members)	\$1,558,355	\$1,749,265
UAAL as a percentage of covered payroll	20.6%	9.1%

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 12 – OTHER POST EMPLOYMENT BENEFITS (Continued)

Actuarial Methods and Assumptions. Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point and do not explicitly reflect the potential effect of legal or contractual funding limitation. The actuarial methods and assumptions used include techniques that are designed to reduce the effect of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the December 31, 2011 actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 4% interest discount rate. The projected annual medical trend rate is 10%. The ultimate medical trend rate is 4.5%. The medical trend rate is reduced 0.5% each year until reaching the 4.5% ultimate trend rate.

Mortality rates are from the RP-2000 Combined Mortality Table projected to 2010 using Scale AA. The salary increase rate was assumed to be 3% per year. The UAAL is being amortized as a level dollar amount on an open basis over 30 years.

Note 13 - RISK MANAGEMENT

The Electric Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Utility assumes liability for any deductible and claims in excess of coverage limits. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. The Utility, as is typical in the electric power industry, does not insure its transmission or distribution lines due to the high cost of such coverage.

Note 14 - RELATED PARTIES

The Electric Utility, Water Utility and Communications Utility of the City of Spencer, Iowa exchange services in the normal course of business.

Two members of the Board of Trustees hold non-controlling interests in a financial institution where the Utility maintains cash balances.

Additional related party items are included in Notes 6 and 10.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 15 - COMMITMENTS

Beginning in 2009, the Electric Utility pledged support to the Iowa Great Lakes Corridor of Opportunity at a level of \$25,000 per year for four years. This commitment is subject to annual review by the Utility Board.

In October 2010, Spencer Municipal Utilities entered into a contract with Midstates Builders, Inc. The contract entails removal and replacement of the damaged portion of the 520 2nd Ave East building roof; provide new foundation, building frames and structures as needed. The original contract amount was \$555,457 with project completion scheduled for September 2011. The final contract amount is \$952,462 and work was completed as of February 2012. The increase was due to improvements made for the space leased to the Iowa Lakes Corridor, additional roof restructuring and new foundation and trenching.

Beginning in 2011, the Electric Utility signed an advertising and signage agreement with the Clay County Regional Event Center. The agreement is effective September 1, 2011 and terminates on August 31, 2014. The annual amount due is \$5,950. A portion of the annual cost is split between the Water and Communications Utility. The Electric Utility is responsible for \$2,677.50 of the annual amount due.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
FUNDING PROGRESS FOR THE RETIREE HEALTH PLAN
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2011**

Year Ended December 31,	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2008	12/31/2008	\$ -	\$ 133,585	\$ 133,585	0%	\$ 1,648,850	8.1%
2009	12/31/2009	\$ -	\$ 142,863	\$ 142,863	0%	\$ 1,698,315	8.4%
2010	12/31/2010	\$ -	\$ 160,019	\$ 160,019	0%	\$ 1,749,265	9.1%
2011	12/31/2011	\$ -	\$ 320,816	\$ 320,816	0%	\$ 1,558,355	20.6%

See Note 12 to the accompanying Notes to Financial Statements for the plan description, funding policy, annual OPEB Cost and Net OPEB Obligation, and the funded status and funding progress.

SUPPLEMENTAL INFORMATION

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS
AND CHANGES IN NET ASSETS - BUDGET AND ACTUAL (CASH BASIS)
OTHER SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2011**

	Budgeted Amounts		Actual	Final to Actual Variance
	Original	Amended		
Receipts:				
Municipal Electric Utility			\$ 22,523,494	
Municipal Water Utility			1,708,171	
Municipal Communications Utility			5,558,166	
Total Receipts	<u>\$ 26,395,419</u>	<u>\$ 30,589,200</u>	<u>29,789,831</u>	<u>\$ (799,369)</u>
Expenditures:				
Municipal Electric Utility			20,718,708	
Municipal Water Utility			1,832,905	
Municipal Communications Utility			7,490,132	
Total Expenditures	<u>27,672,300</u>	<u>35,451,228</u>	<u>30,041,745</u>	<u>5,409,483</u>
Net Change in Net Assets	(1,276,881)	(4,862,028)	(251,914)	4,610,114
Net Assets at Beginning of Year	<u>19,184,020</u>	<u>19,184,020</u>	<u>19,184,020</u>	<u>-</u>
Net Assets at End of Year	<u>\$ 17,907,139</u>	<u>\$ 14,321,992</u>	<u>\$ 18,932,106</u>	<u>\$ 4,610,114</u>

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGET TO GAAP RECONCILIATION
OTHER SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2011**

	Cash Basis	Accrual Adjustments	Accrual Basis
Receipts:			
Municipal Electric Utility	\$ 22,523,494	\$ (8,630,637)	\$ 13,892,857
Municipal Water Utility	1,708,171	113,047	1,821,218
Municipal Communications Utility	5,558,166	229,008	5,787,174
Total Receipts	<u>29,789,831</u>	<u>(8,288,582)</u>	<u>21,501,249</u>
Expenditures:			
Municipal Electric Utility	20,718,708	(7,059,052)	13,659,656
Municipal Water Utility	1,832,905	(318,842)	1,514,063
Municipal Communications Utility	7,490,132	(1,496,869)	5,993,263
Total Expenditures	<u>30,041,745</u>	<u>(8,874,763)</u>	<u>21,166,982</u>
Net Change in Net Assets	(251,914)	586,181	334,267
Net Assets at Beginning of Year	<u>19,184,020</u>	<u>41,879,387</u>	<u>61,063,407</u>
Net Assets at End of Year	<u><u>\$ 18,932,106</u></u>	<u><u>\$ 42,465,568</u></u>	<u><u>\$ 61,397,674</u></u>

See Accompanying Independent Auditors' Report

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
OTHER SUPPLEMENTARY INFORMATION –
BUDGETARY REPORTING
YEAR ENDED DECEMBER 31, 2011**

In accordance with the Code of Iowa, Spencer Municipal Utilities annually adopts a combined budget on the cash basis for the Municipal Electric Utility, Municipal Water Utility, and Municipal Communications Utility of the City of Spencer, Iowa following required public notice and hearing. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures. Encumbrances are not recognized and appropriations lapse at year-end.

Formal and legal budgetary control is based upon nine major classes of disbursements, known as functions, not by fund. These functions are public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects, and business type activities. All Utility disbursements are included in business type activities function and are required to be budgeted.



**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER
MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

Board of Trustees
Spencer Municipal Utilities – Municipal Electric Utility
Spencer, Iowa 51301

We have audited the basic financial statements of Municipal Electric Utility of the City of Spencer, Iowa (Spencer Municipal Utility) as of and for the year ended December 31, 2011, and have issued our report thereon dated April 4, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Spencer Municipal Utility's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting described in Part II of the accompanying Schedule of Findings and as item II-A-11 to be a significant deficiency in internal control over financial reporting. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Spencer Municipal Utility's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

Spencer Municipal Utility's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the Spencer Municipal Utility's responses, we did not audit Spencer Municipal Utility's responses, and accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the City of Spencer and other parties to whom Spencer Municipal Utilities may report. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Spencer Municipal Utilities during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Williams & Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 4, 2012

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL ELECTRIC UTILITY
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2011**

Part I: Summary of the Independent Auditors' Results:

- (a) An unqualified opinion was issued on the financial statements.
- (b) Significant deficiency in internal control over financial reporting was disclosed by the audit of the financial statements.
- (c) The audit did not disclose any noncompliance, which is material to the financial statements.

Part II: Findings Related to the General Purpose Financial Statements

SIGNIFICANT DEFICIENCY:

II-A-11 Financial Reporting – During the audit, we identified immaterial amounts of depreciation expense, bond premium, and amortization expense not initially identified by Spencer Municipal Utility's internal control. These amounts were either not recorded or not properly recorded in Spencer Municipal Utility's financial statements. Adjustments were subsequently made by Spencer Municipal Utility, if applicable, to properly include or reclassify these amounts in the financial statements.

Recommendation – Spencer Municipal Utility should implement procedures to ensure all accounts are properly identified, classified, and included in Spencer Municipal Utility's financial statements.

Response – We will revise our current procedures to ensure the proper amounts are recorded in the financial statements in the future.

Conclusion - Response accepted.

INSTANCES OF NONCOMPLIANCE:

No matters were reported.

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL ELECTRIC UTILITY
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2011**

Part III: Other Findings Related to Required Statutory Reporting

III-A-11 Certified Budget – Disbursements during the year ended December 31, 2011 did not exceed the amounts budgeted in the business type activities function.

III-B-11 Questionable Expenditures – No expenditures were noted which did not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

III-C-11 Travel Expenses – No expenditures of the Utility's money for travel expenses of spouses of Utility's officials or employees were noted.

III-D-11 Business Transactions – Business transactions between Utility and Utility officials and employees are detailed as follows:

<u>Name, Title and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u>
Tom Howe, Board Member Part owner of H & N Chevrolet	Maintenance & Repairs	\$ 41
Dave Hultgren, Board Member Owner, Northwest Equipment	Maintenance & Repairs	\$ 29

(1) These transactions do not appear to represent a conflict of interest since the total transaction was less than \$1,500 during the year, per Chapter 362.5(10) of the Code of Iowa.

III-E-11 Bond Coverage – Surety bond coverage of Spencer Municipal Utilities' officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

III-F-11 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.

III-G-11 Revenue Bonds – As of December 31, 2011 the Utility is in compliance with all bond covenant requirements.

III-H-11 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12(B) and 12(c) of the Code of Iowa and the Utility's investment policy were noted.

SPENCER MUNICIPAL UTILITIES

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA**

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INDEPENDENT AUDITORS' REPORT

Board of Trustees
Spencer Municipal Utilities – Municipal Water Utility
Spencer, IA 51301

We have audited the accompanying financial statements of The Municipal Water Utility of the City of Spencer, Iowa (the Utility), as of and for the year ended December 31, 2011. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year comparative information has been derived from the Utility's 2010 financial statements and, in our report dated April 5, 2011, we expressed an unqualified opinion on the respective financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Utility as of December 31, 2011 and the respective changes in financial position and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 4, 2012, on our consideration of the Utility's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Funding Progress for the Retiree Health Plan information on pages 36 through 38 and page 56 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements taken as a whole. The supplementary information included on pages 57 through 59 is presented for purposes of additional analysis and is not a required part of the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Williams + Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 4, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS

The purpose of Management's Discussion and Analysis (MD&A) is to provide the reader with an introduction to the financial statements. Our discussion and analysis of the Municipal Water Utility (Utility) of the City of Spencer, Iowa's financial performance provides an overview of the Utility's financial activities for the years ended December 31, 2011 and 2010.

The following information should be read in conjunction with the financial statements and the accompanying notes to the financial statements that follow this section.

2011 Financial Highlights

The Utility delivered approximately 418,896,000 gallons of water to its retail customers in 2011 compared to approximately 395,372,000 gallons in 2010.

The Utility's net assets increased by \$307,155 to \$7,101,703 as a result of operations for the year ended December 31, 2011.

Overview of the Financial Statements

The balance sheets include the Utility's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities).

The statement of revenues, expenses and changes in net assets report all revenues and expenses incurred during the fiscal year.

The Statement of Cash Flows present cash receipts, cash disbursements, and net changes in cash resulting from operations, capital and related financing activities and investing activities.

The notes to the financial statements provide the required disclosures and other information that is necessary to give the reader a complete understanding of the data provided in the statements. The notes present information about the Utility's accounting policies, material risks, obligations, commitments, contingencies and subsequent events.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Condensed Financial Information

The following condensed financial information serves as the key financial data and indicators for management, monitoring, and planning.

Condensed Balance Sheet

	<u>2011</u>	<u>2010</u>
Current assets	\$1,519,281	\$1,522,064
Noncurrent assets	1,000,000	1,000,000
Capital assets, net of depr.	6,165,579	5,790,852
Deferred costs	<u>6,976</u>	<u>8,200</u>
Total assets	<u>8,691,836</u>	<u>8,321,116</u>
Current liabilities	779,133	641,568
Long-term debt	<u>811,000</u>	<u>885,000</u>
Total liabilities	<u>1,590,133</u>	<u>1,526,568</u>
Investments in capital assets, net of related debt	5,280,579	4,833,852
Restricted	174,557	170,206
Unrestricted	<u>1,646,567</u>	<u>1,790,490</u>
Total net assets	<u>7,101,703</u>	<u>6,794,548</u>
Total liabilities and net assets	<u>\$8,691,836</u>	<u>\$8,321,116</u>

Condensed Statement of Revenues, Expenses and Changes in Net Assets

Sales of water	\$1,748,373	\$1,490,529
Other	<u>8,575</u>	<u>8,253</u>
Total operating revenue	<u>1,756,948</u>	<u>1,498,782</u>
System operation & maintenance	780,908	928,155
Depreciation & amortization	442,294	401,414
Customer service & administration	<u>186,460</u>	<u>112,442</u>
Total operating expenses	<u>1,409,662</u>	<u>1,442,011</u>
Operating income	347,286	56,771
Interest income	7,446	13,404
Interest expense	(31,183)	(37,634)
Other income (expense)	<u>(16,394)</u>	<u>(26,411)</u>
Total non-operating (expense)	<u>(40,131)</u>	<u>(50,641)</u>
Change in net assets	307,155	6,130
Net assets, beginning of year	<u>6,794,548</u>	<u>6,788,418</u>
Net assets, end of year	<u>\$7,101,703</u>	<u>\$6,794,548</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS

Financial Analysis

The Utility's total assets increased by approximately \$371,000.

The Utility's gross revenues increased by approximately \$258,000 or 17% due to the customer charge in place for the full year of 2011 compared to a half year of 2010. In addition, water sales were on average 6% higher in 2011 compared to 2010 and rates were increased effective with October 2011 consumption.

Total operating expenses decreased by approximately \$32,000 due to decreased expenses related to completion of meter replacement project, reduction of meter reading time and distribution maintenance.

Total operating income generated in 2011 was \$347,286 compared to a \$56,771 gain in 2010.

Contributions in Aid of Construction totaled \$0 for the year ended December 31, 2011 compared to \$9,792 for the year ended December 31, 2010.

The Utility had a net profit of \$307,155 for the year ended December 31, 2011 compared to a net profit of \$6,130 for the year ended December 31, 2010.

Capital Assets and Debt Administration

Net capital assets increased by approximately \$375,000 due to the completion the 2nd Ave E water main construction and replacement of roof and repainting of the 1.5 million gallon water storage tank during the year ended December 31, 2011.

Economic Factors

During the year ended December 31, 2011, the Utility experienced a net profit of \$307,155. The rate adjustment effective with consumption beginning October 1, 2011 in addition to a full year of collecting the customer charge that was implemented in June of 2010 allowed the Utility sufficient coverage of operational and non-operational expenses. Management will continue to monitor the operations of the Utility in addition to projected capital expenditures and propose rate adjustments accordingly.

Contacting the Utility's Financial Management

This financial report is designed to present our citizens, customers, and creditors with a general overview of the Utility's finances and operating activities. If you have any questions or require additional information please contact the Finance Manager, 712 Grand Ave, PO Box 222, Spencer, Iowa 51301.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF NET ASSETS
DECEMBER 31, 2011 AND 2010**

	2011	2010
ASSETS		
Current Assets:		
Cash and Cash Equivalents		
Unrestricted	\$ 162,284	\$ 146,480
Board Designated	579,106	719,106
Restricted	174,557	170,206
Accounts Receivable (Net of Allowance for Doubtful Accounts of \$2,500 and \$2,000)	487,797	336,471
Unbilled Usage	31,985	69,993
Materials and Supplies Inventory	74,211	70,820
Prepayments and Other	9,341	8,988
Total Current Assets	1,519,281	1,522,064
Capital Assets:		
Land	258,533	258,533
Construction in Progress	58,504	103,734
Plant in Service	13,225,740	12,412,628
Accumulated Depreciation	(7,377,198)	(6,984,043)
Total Capital Assets	6,165,579	5,790,852
Noncurrent Assets:		
Noncurrent Investments		
Board Designated	1,000,000	1,000,000
Unamortized Bond Issue Costs	6,976	8,200
Total Noncurrent Assets	1,006,976	1,008,200
Total Assets	\$ 8,691,836	\$ 8,321,116

See Accompanying Notes to Financial Statements

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF NET ASSETS
DECEMBER 31, 2011 AND 2010**

	2011	2010
LIABILITIES		
Current Liabilities:		
Accounts Payable	\$ 670,478	\$ 532,263
Payroll and Sales Tax Payable	9,753	9,580
Accrued Payroll and Compensated Absences	20,501	21,634
Accrued Interest Payable	4,401	6,091
Current Maturities of Long-Term Debt	74,000	72,000
Total Current Liabilities	<u>779,133</u>	<u>641,568</u>
Bonds Payable:		
Bonds Payable	885,000	957,000
Less - Current Maturities	<u>(74,000)</u>	<u>(72,000)</u>
Total Bonds Payable	<u>811,000</u>	<u>885,000</u>
Total Liabilities	<u>1,590,133</u>	<u>1,526,568</u>
NET ASSETS		
Net Assets		
Invested in Capital Assets, Net of Related Debt	5,280,579	4,833,852
Restricted	174,557	170,206
Unrestricted	<u>1,646,567</u>	<u>1,790,490</u>
Total Net Assets	<u>\$ 7,101,703</u>	<u>\$ 6,794,548</u>

See Accompanying Notes to Financial Statements

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**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	2011	2010
Operating Revenues:		
Residential	\$ 1,237,324	\$ 1,050,837
Commercial	511,049	439,692
Service Permits	5,975	7,100
Miscellaneous	2,600	1,153
Total Operating Revenues	1,756,948	1,498,782
Operating Expenses:		
Treatment	548,330	434,154
Distribution	232,578	494,001
Depreciation and Amortization	442,294	401,414
Customer Operations	26,110	26,771
General and Administrative	160,350	85,671
Total Operating Expenses	1,409,662	1,442,011
Operating Income	347,286	56,771
Non-Operating Income (Expense):		
Interest Income on Investments	7,446	13,404
Contributions From Developers	-	9,792
Resource Conservation	4,889	(19,069)
Leased Facilities	35,715	37,353
Interest Expense	(29,959)	(37,634)
Bond Amortization Expense	(1,224)	(1,224)
Inventory Sales	280	5,453
Gain on Plant Retirements	15,940	-
Payment in Lieu of Property Taxes	(73,218)	(58,716)
Total Non-Operating Income (Expense)	(40,131)	(50,641)
Change in Net Assets	307,155	6,130
Net Assets at Beginning of Year	6,794,548	6,788,418
Net Assets at End of Year	\$ 7,101,703	\$ 6,794,548

See Accompanying Notes to Financial Statements

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
Cash Flows From Operating Activities:		
Cash Received From Customers	\$ 1,643,630	\$ 1,354,253
Cash Payments to Suppliers for Goods and Services	(479,688)	(683,645)
Cash Payments to Employees for Services	(354,168)	(446,591)
Cash Payments In Lieu of Property Taxes	(73,218)	(58,716)
Cash Payments for Resource Conservation	4,889	(19,069)
Payments Received From Leasing of Facilities	35,715	37,353
	<hr/>	<hr/>
Net Cash Provided By Operating Activities	777,160	183,585
	<hr/>	<hr/>
Cash Flows From Capital and Related Financing Activities:		
Acquisition & Construction of Property and Equipment	(822,182)	(361,771)
Proceeds from Sale of Capital Assets	21,100	-
Revenue Bond Principal Repayment	(72,000)	(69,000)
Payments Received From Sale of Inventory	280	5,453
Interest Paid	(31,649)	(38,073)
	<hr/>	<hr/>
Net Cash (Used) By Capital and Related Financing Activities	(904,451)	(463,391)
	<hr/>	<hr/>
Cash Flows From Investing Activities:		
Interest Received From Investments	7,446	13,404
	<hr/>	<hr/>
Net Cash Provided By Investing Activities	7,446	13,404
	<hr/>	<hr/>
Net (Decrease) in Cash	(119,845)	(266,402)
	<hr/>	<hr/>
Cash and Cash Equivalents at Beginning of Year	1,035,792	1,302,194
	<hr/>	<hr/>
Cash and Cash Equivalents at End of Year	\$ 915,947	\$ 1,035,792
	<hr/>	<hr/>
Reconciliation:		
Cash and Cash Equivalents		
Unrestricted	\$ 162,284	\$ 146,480
Restricted	174,557	170,206
Board Designated	579,106	719,106
	<hr/>	<hr/>
	\$ 915,947	\$ 1,035,792
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See Accompanying Notes to Financial Statements

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	2011	2010
Reconciliation of Operating Income to Net Cash Provided by Operating Activities		
Operating Income	\$ 347,286	\$ 56,771
Adjustments to Reconcile Operating Income to Net Cash Provided By Operating Activities		
Depreciation and Amortization	442,294	401,414
Leased Facilities Income	35,715	37,353
Payment in Lieu of Property Taxes	(73,218)	(58,716)
Payment for Resource Conservation	4,889	(19,069)
(Increase) Decrease in Operating Assets:		
Accounts Receivable	(151,326)	(118,363)
Unbilled Usage	38,008	(26,166)
Materials and Supplies Inventory	(3,391)	(2,711)
Prepayments	(353)	(2,421)
Increase (Decrease) in Operating Liabilities:		
Accounts Payable	138,216	(96,877)
Accrued Payroll and Compensated Absences	(960)	12,370
Total Adjustments	429,874	126,814
Net Cash Provided By Operating Activities	\$ 777,160	\$ 183,585

See Accompanying Notes to Financial Statements

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Basis of Accounting

The Municipal Water Utility of the City of Spencer, Iowa (Water Utility or Utility) operates as an independent unit of the City of Spencer and is managed, along with the Municipal Electric Utility and the Municipal Communication Utility of the City of Spencer, Iowa by a five member Board of Trustees.

The Utility follows the accounting practices prescribed through the Federal Energy Regulatory Commission for regulated utilities and proprietary fund accounting for governmental entities under accounting principles generally accepted in the United States of America.

For financial reporting purposes, the Utility has included all funds. The Utility has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Utility are such that exclusion would cause the Utility's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Utility to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Utility. It was determined that the Utility has no component units.

The Utility is not considered to be a component unit of the City of Spencer for financial statement purposes.

The Utility's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

In reporting the financial activity of its enterprise fund, the Utility applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure.

The Utility distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. The principal operating revenues of the Utility are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Capital Assets and Depreciation

Capital assets are stated at original cost when first devoted to public service. Currently, such costs include labor-related expenditures, such as payroll taxes, pensions, and other fringe benefits and administrative costs for labor related to the construction of new water facilities. In addition, net interest costs on construction debt are capitalized.

Replacements and betterments of capital assets are charged to capital assets. Routine maintenance and repairs are charged to expense as incurred.

Depreciation is provided on a straight-line basis. Current depreciation expense is approximately 3.34% of the original cost of depreciable water plant in service.

The estimated useful lives used to depreciate assets by class are as follows:

Infrastructure	40 years
Buildings and Equipment	5-20 years
Vehicles	5 years

C. Accounts Receivable

Accounts receivable are stated at the amount the Utility expects to collect from outstanding balances. The Utility provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after the Utility has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements.

D. Inventories

Inventories are valued at the lower of cost or market. The average cost method is used for determining the cost of materials and supplies inventory. Inventories are recorded as an expenditure or, if applicable, capitalized when consumed.

E. Unamortized Bond Issue Costs

Unamortized debt issue costs are amortized over the life of the debt on a straight line basis which approximates the effective interest method.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

F. Net Assets

Net assets represent the difference between assets and liabilities in the financial statements. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used for acquisition, construction or improvement of those assets and increased by unspent debt when there are limitations imposed on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

The Utility's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

G. Income Taxes

The Water Utility is exempt from federal and state income taxes because it is a governmental entity organized under the provisions of Chapter 388 of the Code of Iowa.

H. Revenues and Unbilled Usage

Revenues are based on billing rates, which are applied to customers' consumption of water. The Utility records estimated unbilled revenue at the end of accounting periods. Revenues earned, but not yet billed at December 31, 2011 and 2010 totaled \$31,985 and \$69,993, respectively.

I. Estimates

The preparation of the financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

Note 2 - CASH AND CASH EQUIVALENTS AND NONCURRENT INVESTMENTS

The Utility's deposits in bank at December 31, 2011 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Utility is authorized by statute and Board of Trustees' approval to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit and other evidences of deposit at federally insured Iowa depository institutions; and the Iowa Public Agency Investment Trust.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 2 - CASH AND CASH EQUIVALENTS AND NONCURRENT INVESTMENTS (Continued)

Interest Rate Risk – The Utility’s investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days, but the maturities shall be consistent with the needs and use of the Utility.

Credit Risk –The Utility considers all highly liquid investments with an original maturity of three months or less to be cash equivalents for purposes of the statement of cash flows.

Investments are recorded at cost which approximates market. Adjustments are made to cost for any premium or discount, which is amortized over the maturity of the investment. Adjustments are also made to account for the change in accrued interest on respective investments.

Reconciliation of the Utility’s cash and cash equivalents and noncurrent investments is as follows:

Cash and cash equivalents:	2011	2010
Board designated	\$ 579,106	\$ 719,106
Restricted	174,557	170,206
Unrestricted	162,284	146,480
Total cash and cash equivalents	915,947	1,035,792
Noncurrent investments:		
Board designated	1,000,000	1,000,000
Total noncurrent investments	1,000,000	1,000,000
Total cash and cash equivalents and noncurrent investments	\$ 1,915,947	\$ 2,035,792

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 3 - BOARD DESIGNATED FUNDS

The Board of trustees of the Utility has designated certain funds to be placed in a contingency reserve account. These funds, which are from unrestricted net assets, are being designated for contingencies such as a natural disaster and cannot be expended without Board approval.

The Board of Trustees of the Utility has designated certain funds to be placed in a replacement and construction reserve account. These funds, which are from unrestricted net assets, are being designated for replacement of property, plant, and equipment and for new construction. These funds cannot be expended without Board approval.

Assets of the funds as of December 31, 2011 are summarized as follows:

	Contingency Reserve	Replacement and Construction Reserve	Total
Cash and cash equivalents	\$ 469,106	\$ 110,000	\$ 579,106
Noncurrent investments	-	1,000,000	1,000,000
Total	<u>\$ 469,106</u>	<u>\$ 1,110,000</u>	<u>\$ 1,579,106</u>

Assets of the funds as of December 31, 2010 are summarized as follows:

	Contingency Reserve	Replacement and Construction Reserve	Total
Cash and cash equivalents	\$ 469,106	\$ 250,000	\$ 719,106
Noncurrent investments	-	1,000,000	1,000,000
Total	<u>\$ 469,106</u>	<u>\$ 1,250,000</u>	<u>\$ 1,719,106</u>

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 4 - CAPITAL ASSETS

Capital assets activity for the year ended December 31, 2011 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 258,533	\$ -	\$ -	\$ 258,533
Construction in progress	103,734	58,504	(103,734)	58,504
Total capital assets not being depreciated	362,267	58,504	(103,734)	317,037
Capital assets being depreciated:				
Infrastructure	7,797,308	359,896	-	8,157,204
Buildings and equipment	4,407,091	396,515	-	4,803,606
Vehicles	208,229	111,000	(54,299)	264,930
Total capital assets being depreciated	12,412,628	867,411	(54,299)	13,225,740
Less accumulated depreciation	6,984,043	442,295	(49,140)	7,377,198
Total capital assets being depreciated - net	5,428,585	425,116	(5,159)	5,848,542
Capital assets - net	\$ 5,790,852	\$483,620	\$(108,893)	\$ 6,165,579

Capital assets activity for the year ended December 31, 2010 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 258,533	\$ -	\$ -	\$ 258,533
Construction in progress	-	103,734	-	103,734
Total capital assets not being depreciated	258,533	103,734	-	362,267
Capital assets being depreciated:				
Infrastructure	7,590,259	207,049	-	7,797,308
Buildings and equipment	4,346,311	60,780	-	4,407,091
Vehicles	208,229	-	-	208,229
Total capital assets being depreciated	12,144,799	267,829	-	12,412,628
Less accumulated depreciation	6,582,629	401,414	-	6,984,043
Total capital assets being depreciated - net	5,562,170	(133,586)	-	5,428,585
Capital assets - net	\$ 5,820,703	\$ (29,852)	\$ -	\$ 5,790,852

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 5 - SEWER, STORM WATER, AND SOLID WASTE

The Electric Utility bills and collects sewer, storm water, and solid waste revenues for the City of Spencer. The resulting receivable and corresponding payable are recorded under the Water Utility. The City of Spencer reimburses the Electric Utility for these services.

Note 6 - TRANSFERS IN LIEU OF PROPERTY TAXES

By resolution of the Board of Trustees, voluntary transfers in lieu of property taxes are made to the City of Spencer, Iowa. Currently, transfers approximate 5% of gross sales. Additionally, funds declared to be surplus can be, and have been, transferred to the City.

Note 7 – BONDS PAYABLE

Bonds payable activity for the year ended December 31, 2011 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Series 2000 revenue bonds	\$957,000	\$ -	\$ 72,000	\$885,000	\$ 74,000

Bonds payable activity for the year ended December 31, 2010 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Series 2000 revenue bonds	\$1,026,000	\$ -	\$ 69,000	\$957,000	\$ 72,000

The Series 2000 revenue bonds require annual principal payments, due December 1, and semiannual interest payments, due June 1 and December 1. Interest rate through May 1st, 2011 is 3.84%. Effective May 1st, 2011 throughout the term of the bonds is 3.00%. The bonds are secured by the future net revenues of the Utility. Long-term debt matures and bears interest as follows:

	Series 2000	
	Principal	Interest
2012	\$ 74,000	\$ 25,440
2013	77,000	23,175
2014	80,000	20,820
2015	83,000	18,375
2016	86,000	15,840
2017-2021	485,000	37,455
Total	\$ 885,000	\$ 141,105

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 7 – BONDS PAYABLE (Continued)

The bond resolutions provide certain covenants relating to the collection, segregation, and distribution of revenues from customers; places certain restrictions on future borrowing and leasing or disposition of assets; and requires that minimum insurance coverage be maintained.

Revenue Bonds

The Utility has pledged future utility revenue, net of specified operating expenses, to repay outstanding utility revenue bonds. The bonds are payable solely from the utility's net revenues and are payable through 2021. The total principal and interest remaining to be paid on the bonds is \$1,026,105. Principal and interest paid for the current year and total combined utilities net revenues were \$110,074 and 789,580, respectively.

Restricted Funds

Outstanding Water Revenue Bonds are collateralized by the revenue of the Utility and the various special funds established by bond covenants. The covenants provide that the revenue of the Utility is to be used first to pay operating and maintenance expenses of the system and second to establish and maintain the special funds. Remaining revenues may then be used for any lawful purpose. The covenants also contain provisions which, among other items, restrict the issuance of additional revenue bonds unless the special funds noted above contain the required amounts and certain financial ratios are met. As of December 31, 2011 and 2010 the Utility is in compliance with all bond covenant requirements except the Net Revenue requirement.

The special funds consisted of the following:

	2011	2010
Bond Sinking Fund	\$ 59,557	\$ 55,206
Bond Reserve Fund	115,000	115,000
Total	<u>\$ 174,557</u>	<u>\$ 170,206</u>

Monthly deposits into the bond sinking fund are required to establish the amount necessary to pay the next installments of principal and interest. The bond reserve fund at December 31, 2011 and 2010 equaled the required balance; therefore monthly deposits into the fund are not currently required. These funds may be used to pay principal and interest payments when insufficient funds are available in the sinking fund.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 8 - RATE MATTERS

Rates of the Utility are established by the Board of Trustees and, as a municipal system, are not subject to the regulation of the Utilities Division of the Department of Commerce of the State of Iowa.

Note 9 - NUMBER OF METER CONNECTIONS

The number of meter connections totaled 5,850 and 5,826 at December 31, 2011 and 2010, respectively.

Note 10 - LEASES

The Utility leases building space to the Electric Utility and Communications Utility. The revenues from such leases are classified as leased facilities. The leases are monthly leases based on building space utilized and totaled \$11,968 in 2011 and 2010. The receivable at December 31, 2011 and 2010 was \$11,968 each year.

The Utility lease bandwidth and building space from the Electric and Communications Utilities. The expense from such leases is classified as operating expense. The lease is a 20-year variable lease based on bandwidth and space utilized and totaled \$23,418 and \$23,418 in 2011 and 2010. The payable at December 31, 2011 and 2010 was \$23,418 and \$23,418, respectively.

Note 11 - RETIREMENT SYSTEM

IPERS

The Utility contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing, multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan member and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, PO Box 9117, Des Moines, Iowa, 50306-9117.

Plan members were required to contribute 4.50% through June 30, 2011 and 5.38% presently of their annual salary and the Utility was required to contribute 6.95% through June 30, 2011 and 8.07% presently of annual payroll. Contribution requirements are established by State statute. The Utility's contributions to IPERS for the years ended December 31, 2011, 2010 and 2009 were \$17,817, \$19,567 and \$19,305, respectively, equal to the required contributions for each year.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 11 - RETIREMENT SYSTEM (Continued)

EMPLOYEES PENSION PLAN

All full-time employees of the Water Utility who have completed six months of continuous employment and are 18 years of age are eligible to participate in a 457b Pension Plan administered by Security National Bank. The Utility contributes 8% of the employees' compensation for all employees contributing at least 2% of their salary.

The Water Utility's contribution to the Money Accumulation Pension Plan for 2011 and 2010 totaled \$16,258 and \$20,599, respectively.

Note 12 – OTHER POST EMPLOYMENT BENEFITS

Plan Description. The Utility operates a single-employer retiree benefit plan which provides medical/prescription drug benefits for retirees and their family.

The medical/prescription drug coverage is provided through a fully-insured plan. Retirees under age 65 pay the same premium for the medical/prescription drug benefit as active employees, which results in an implicit subsidy and an OPEB liability.

Funding Policy. The Utility currently finances the retiree benefit plan on a pay-as-you-go basis.

Annual OPEB Cost and NET OPEB Obligation. The Utility's annual other post-employment benefit (OPEB) cost is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty years.

The following table shows the components of the Utility's annual OPEB for the year, the amount actually contributed to the plan, and changes in the Utility's net OPEB obligation to the plan:

	<u>2011</u>	<u>2010</u>
Annual required contribution	\$ 2,498	\$ 2,431
Interest on net OPEB obligation	262	166
Adjustment to annual required contribution	<u>(261)</u>	<u>(164)</u>
Annual OPEB cost (Expense)	2,499	2,433
Contributions made	<u>0</u>	<u>(13)</u>
Increase in net OPEB obligation	2,499	2,420
Net OPEB obligation – beginning of year	<u>6,558</u>	<u>4,138</u>
Net OPEB obligation – end of year	<u>\$ 9,057</u>	<u>\$ 6,558</u>

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 12 – OTHER POST EMPLOYMENT BENEFITS (Continued)

The Utility's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation were as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2011	\$ 2,499	0%	\$ 9,057
2010	\$ 2,433	1%	\$ 6,558

Funded Status and Funding Progress. The funded status of the plan as of December 31, 2011 was as follows:

	2011	2010
Actuarial accrued liability (AAL)	\$ 14,137	\$ 16,680
Actuarial value of plan assets	-	-
Unfunded actuarial accrued liability (UAAL)	<u>\$ 14,137</u>	<u>\$ 16,680</u>
Covered payroll (active members)	\$258,674	\$382,033
UAAL as a percentage of covered payroll	5.5%	4.4%

Actuarial Methods and Assumptions. Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point and do not explicitly reflect the potential effect of legal or contractual funding limitation. The actuarial methods and assumptions used include techniques that are designed to reduce the effect of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the December 31, 2011 actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 4% interest discount rate. The projected annual medical trend rate is 10%. The ultimate medical trend rate is 4.5%. The medical trend rate is reduced 0.5% each year until reaching the 4.5% ultimate trend rate.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 12 – OTHER POST EMPLOYMENT BENEFITS (Continued)

Mortality rates are from the RP-2000 Combined Mortality Table projected to 2010 using Scale AA. The salary increase rate was assumed to be 3% per year. The UAAL is being amortized as a level dollar amount on an open basis over 30 years.

Note 13 - RISK MANAGEMENT

The Water Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Utility assumes liability for any deductible and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Note 14 - RELATED PARTIES

The Electric Utility, Water Utility, and Communications Utility of the City of Spencer, Iowa exchange services in the normal course of business.

Two members of the Board of Trustees hold non-controlling interests in a financial institution where the Utility maintains cash balances.

Additional related party items are included in Note 10.

Note 15 – COMMITMENTS

Spencer Municipal Utilities entered into an agreement with Valley Contracting, Inc., in July 2011. The contract is in the amount of \$276,977 for improvements to water mains located by City RR Track, 2nd Avenue E and E 7th Street and 2nd Avenue E. The improvements included main replacement of approximately 2,700 lineal feet ranging from 4" to 8" pipe. Project completion should occur no later than August 1, 2012.

Beginning in 2011, the Water Utility signed an advertising and signage agreement with the Clay County Regional Event Center. The agreement is effective September 1, 2011 and terminates on August 31, 2014. The annual amount due is \$5,950. A portion of the annual cost is split between the Electric and Communications Utility. The Water Utility is responsible for \$595 of the annual amount due.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
FUNDING PROGRESS FOR THE RETIREE HEALTH PLAN
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2011**

Year Ended December 31,	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2008	12/31/2008	\$ -	\$ 11,713	\$ 11,713	0%	\$ 360,103	3.3%
2009	12/31/2009	\$ -	\$ 13,726	\$ 13,726	0%	\$ 370,906	3.7%
2010	12/31/2010	\$ -	\$ 16,680	\$ 16,680	0%	\$ 382,033	4.4%
2011	12/31/2011	\$ -	\$ 14,137	\$ 14,137	0%	\$ 258,674	5.5%

See Note 12 to the accompanying Notes to Financial Statements for the plan description, funding policy, annual OPEB Cost and Net OPEB Obligation, and the funded status and funding progress.

SUPPLEMENTAL INFORMATION

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS
AND CHANGES IN NET ASSETS - BUDGET AND ACTUAL (CASH BASIS)
OTHER SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2011**

	Budgeted Amounts		Actual	Final to Actual Variance
	Original	Amended		
Receipts:				
Municipal Electric Utility			\$ 22,523,494	
Municipal Water Utility			1,708,171	
Municipal Communications Utility			5,558,166	
Total Receipts	<u>\$ 26,395,419</u>	<u>\$ 30,589,200</u>	<u>29,789,831</u>	<u>\$ (799,369)</u>
Expenditures:				
Municipal Electric Utility			20,718,708	
Municipal Water Utility			1,832,905	
Municipal Communications Utility			7,490,132	
Total Expenditures	<u>27,672,300</u>	<u>35,451,328</u>	<u>30,041,745</u>	<u>5,409,483</u>
Net Change in Net Assets	(1,276,881)	(1,962,028)	(251,914)	4,610,114
Net Assets at Beginning of Year	<u>19,184,020</u>	<u>19,184,020</u>	<u>19,184,020</u>	<u>-</u>
Net Assets at End of Year	<u><u>\$ 17,907,139</u></u>	<u><u>\$ 17,221,992</u></u>	<u><u>\$ 18,932,106</u></u>	<u><u>\$ 4,610,114</u></u>

See Accompanying Independent Auditors' Report

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGET TO GAAP RECONCILIATION
OTHER SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2011**

	Cash Basis	Accrual Adjustments	Accrual Basis
Receipts:			
Municipal Electric Utility	\$ 22,523,494	\$ (8,630,637)	\$ 13,892,857
Municipal Water Utility	1,708,171	113,047	1,821,218
Municipal Communications Utility	5,558,166	229,008	5,787,174
Total Receipts	<u>29,789,831</u>	<u>(8,288,582)</u>	<u>21,501,249</u>
Expenditures:			
Municipal Electric Utility	20,718,708	(7,059,052)	13,659,656
Municipal Water Utility	1,832,905	(318,842)	1,514,063
Municipal Communications Utility	7,490,132	(1,496,869)	5,993,263
Total Expenditures	<u>30,041,745</u>	<u>(8,874,763)</u>	<u>21,166,982</u>
Net Change in Net Assets	(251,914)	586,181	334,267
Net Assets at Beginning of Year	<u>19,184,020</u>	<u>41,879,387</u>	<u>61,063,407</u>
Net Assets at End of Year	<u>\$ 18,932,106</u>	<u>\$ 42,465,568</u>	<u>\$ 61,397,674</u>

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO OTHER SUPPLEMENTARY INFORMATION –
BUDGETARY REPORTING
YEAR ENDED DECEMBER 31, 2011**

In accordance with the Code of Iowa, Spencer Municipal Utilities annually adopts a combined budget on the cash basis for the Municipal Electric Utility, Municipal Water Utility, and Municipal Communications Utility of the City of Spencer, Iowa following required public notice and hearing. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures. Encumbrances are not recognized and appropriations lapse at year-end.

Formal and legal budgetary control is based upon nine major classes of disbursements, known as functions, not by fund. These functions are public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects and business type activities function and are required to be budgeted.



Certified Public Accountants

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER
MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

Board of Trustees
Spencer Municipal Utilities – Municipal Water Utility
Spencer, Iowa 51301

We have audited the accompanying financial statements of The Municipal Water Utility of the City of Spencer, Iowa (Spencer Municipal Utility) as of and for the year ended December 31, 2011, which collectively comprise the Utility's basic financial statements listed in the table of contents, and have issued our report thereon dated April 4, 2012. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Spencer Municipal Utility's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting described in Part II of the accompanying Schedule of Findings and as item II-A-11 to be a significant deficiency in internal control over financial reporting. A significant deficiency, is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Spencer Municipal Utility's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

Spencer Municipal Utility's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the Spencer Municipal Utility's responses, we did not audit Spencer Municipal Utility's responses, and accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of Spencer Municipal Utility and other parties to whom Spencer Municipal Utility may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Spencer Municipal Utilities during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Williams + Company, PC
Certified Public Accountants

Spencer, Iowa
April 4, 2012

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL WATER UTILITY
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2011**

Part I: Summary of the Independent Auditors' Results:

- (a) An unqualified opinion was issued on the financial statements.
- (b) Significant deficiency in internal control over financial reporting was disclosed by the audit of the financial statements.
- (c) The audit did not disclose any noncompliance, which is material to the financial statements.

Part II: Findings Related to the General Purpose Financial Statements

SIGNIFICANT DEFICIENCY:

II-A-11 Financial Reporting – During the audit, we identified an immaterial amount of fixed assets not initially identified by Spencer Municipal Utility's internal control. These amounts were either not recorded or not properly recorded in Spencer Municipal Utility's financial statements. Adjustments were subsequently made by Spencer Municipal Utility, if applicable, to properly include or reclassify these amounts in the financial statements.

Recommendation – Spencer Municipal Utility should implement procedures to ensure all accounts are properly identified, classified, and included in Spencer Municipal Utility's financial statements.

Response – We will revise our current procedures to ensure the proper amounts are recorded in the financial statements in the future.

Conclusion - Response accepted.

INSTANCES OF NONCOMPLIANCE:

No matters were reported.

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL WATER UTILITY
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2011**

Part III: Other Findings Related to Required Statutory Reporting

III-A-11 Certified Budget – Disbursements during the year ended December 31, 2011, did not exceed the amounts budgeted in the business type activities function.

III-B-11 Questionable Expenditures – We noted no expenditures that we believe may not meet the requirements of public purpose as defined in an Attorney General’s opinion dated April 25, 1979.

III-C-11 Travel Expenses – No expenditures of Utility’s money for travel expenses of spouses of Utility’s officials or employees were noted.

III-D-11 Business Transactions – Business transactions between Utility and Utility officials and employees are detailed as follows:

<u>Name, Title and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u>
Tom Howe, Board Member Part owner of H & N Chevrolet	Maintenance & Repairs	\$ 119
Dan Schuck, Employee Owner, Accurate Appliance	Equipment	\$ 285

(1) The transaction does not appear to represent a conflict of interest since the total transaction was less then \$1,500 during the year, per Chapter 362.5(10) of the Code of Iowa.

III-E-11 Bond Coverage – Surety bond coverage of Spencer Municipal Utilities’ officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

III-F-11 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.

III-G-11 Revenue Bonds –As of December 31, 2011, the Utility is in compliance with all bond covenant requirements except the Net Revenue requirement.

III-H-11 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12(B) and 12(c) of the Code of Iowa and the Utility’s investment policy were noted.

SPENCER MUNICIPAL UTILITIES
MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA

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INDEPENDENT AUDITORS' REPORT

Board of Trustees
Spencer Municipal Utilities – Municipal Communications Utility
Spencer, IA 51301

We have audited the accompanying financial statements of The Municipal Communications Utility of the City of Spencer, Iowa (the Utility), as of and for the year ended December 31, 2011. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year comparative information has been derived from the Utility's 2010 financial statements and, in our report dated April 5, 2011, we expressed an unqualified opinion on the respective financial statements..

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Utility as of December 31, 2011 and the respective changes in financial position and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 4, 2012, on our consideration of the Utility's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Funding Progress for the Retiree Health Plan Information on pages 66 through 67 and page 83 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements taken as a whole. The supplementary information included on pages 84 through 86 is presented for purposes of additional analysis and is not a required part of the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Williams + Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 4, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS

The purpose of Management's Discussion and Analysis (MD&A) is to provide the reader with an introduction to the financial statements. Our discussion and analysis of the Municipal Communications Utility (Utility) of the City of Spencer, Iowa's financial performance provides an overview of the Utility's financial activities for the years ended December 31, 2011 and 2010.

The following information should be read in conjunction with the financial statements and the accompanying notes to the financial statements that follow this section.

2011 Financial Highlights

Total assets decreased by approximately \$2,335,000 which was attributable to adjusting the allowance based on settlement estimates and amounts due to conference bridge partner.

Total net assets decreased by \$206,089 as the result of the utility operations.

Overview of the Financial Statements

The balance sheets include the Utility's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities).

The statement of revenues, expenses and changes in net assets report all revenues and expenses incurred during the fiscal year.

The Statement of Cash Flows present cash receipts, cash disbursements, and net changes in cash resulting from operations, capital and related financing activities and investing activities.

The notes to the financial statements provide the required disclosures and other information that is necessary to give the reader a complete understanding of the data provided in the statements. The notes present information about the Utility's accounting policies, material risks, obligations, commitments, contingencies and subsequent events.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Condensed Financial Information

The following condensed financial information serves as the key financial data and indicators for management, monitoring, and planning.

Condensed Balance Sheet

	<u>2011</u>	<u>2010</u>
Current assets	\$5,562,429	\$7,258,652
Capital assets, net of depreciation	3,864,152	4,563,215
Noncurrent assets	<u>831,114</u>	<u>771,315</u>
Total assets	<u>10,257,695</u>	<u>12,593,182</u>
Current liabilities	1,196,305	1,323,303
Long-term debt	<u>1,039,600</u>	<u>3,042,000</u>
Total liabilities	<u>2,235,905</u>	<u>4,365,303</u>
Investments in capital assets, net of related debt	2,864,152	1,563,215
Unrestricted	<u>5,157,638</u>	<u>6,664,664</u>
Total net assets	<u>8,021,790</u>	<u>8,227,879</u>
Total liabilities and net assets	<u>\$10,257,695</u>	<u>\$12,593,182</u>

Condensed Statement of Revenues, Expenses and Changes in Net Assets

Cable television revenue	\$2,082,052	\$1,763,505
Telephone revenue	1,985,379	2,291,717
Data revenue	1,434,109	1,352,263
Miscellaneous revenue	<u>14,928</u>	<u>12,797</u>
Total operating revenue	<u>5,516,468</u>	<u>5,420,282</u>
System operation & maintenance	3,464,441	3,774,548
Depreciation & amortization	1,159,384	1,150,833
Customer service & administration	<u>1,174,079</u>	<u>1,137,567</u>
Total operating expenses	<u>5,797,904</u>	<u>6,062,948</u>
Operating (loss)	(281,436)	(642,666)
Interest income	25,335	21,575
Interest expense	(141,788)	(137,800)
Other income (expense)	<u>191,800</u>	<u>(387,906)</u>
Total non-operating revenue (expense)	<u>75,347</u>	<u>(504,131)</u>
Change in net assets	(206,089)	(1,146,797)
Net assets, beginning of year	<u>8,227,879</u>	<u>9,374,676</u>
Net assets, end of year	<u>\$8,021,790</u>	<u>\$8,227,879</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS

Financial Analysis

The Utility's total assets decreased by approximately \$2,335,000.

The Utility's gross revenues increased by approximately \$96,000 or 2% due to the rate increase on basic plus cable effective 11/01/2011. Revenue also increased due to an 11/01/2011 residential internet rate increase as well as a 6% increase in residential internet subscriber count. Also impacting the increase in gross revenues was the approximately 25% increase in Digital and DVR subscriber counts.

Total operating expenses decreased by approximately \$265,000 due to a decrease in the Zone switching expense and loss of ADC support maintenance.

Total operating loss in 2011 was approximately (\$281,436) compared to approximately (\$642,666) in 2010.

The Utility had a net loss of (\$206,089) for the year ended December 31, 2011 compared to a net loss of (\$1,146,797) for the year ended December 31, 2010. The change was attributable to the Qwest access write off from 2010 in addition to significant decrease in the lieu of tax payment in 2011 compared to 2010.

Capital Assets and Debt Administration

Net capital assets decreased by approximately \$699,000 and \$687,000 for years ending December 31, 2011 and 2010, respectively. This was due to depreciation exceeding assets placed in service for both years ending December 31, 2011 and 2010.

Economic Factors

The Utility continues to see stable growth in subscriber base. The Utility will be faced with increased costs of operating due to cable programming contracts. Although the Verizon and Global Crossing lawsuit was settled, uncertainty remains as to the outcome of legal litigation concerning collectable access revenues with Sprint, AT&T and Qwest. Management remains conservative in estimating access collectable balance.

Contacting the Utility's Financial Management

This financial report is designed to present our citizens, customers, and creditors with a general overview of the Utility's finances and operating activities. If you have any questions or require additional information please contact the Finance Manager, 712 Grand Ave, PO Box 222, Spencer, Iowa 51301.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF NET ASSETS
DECEMBER 31, 2011 AND 2010**

	2011	2010
ASSETS		
Current Assets:		
Cash and Cash Equivalents	\$ 3,330,322	\$ 5,262,288
Consumer Deposits	61,023	63,028
Accounts Receivable	1,724,778	1,597,761
Unbilled Usage	238,221	201,220
Materials And Supplies Inventory	96,545	85,685
Prepayments and Other	111,540	48,670
Total Current Assets	5,562,429	7,258,652
Capital Assets:		
Land	10,342	10,342
Property and Equipment	13,067,728	12,612,204
Accumulated Depreciation	(9,213,918)	(8,059,331)
Total Capital Assets	3,864,152	4,563,215
Noncurrent Assets:		
Unamortized Bond Issue Costs	1,200	5,996
Long-term Receivables	829,914	765,319
Total Noncurrent Assets	831,114	771,315
Total Assets	10,257,695	12,593,182
LIABILITIES		
Current Liabilities:		
Accounts Payable	1,018,258	1,152,900
Payroll and Sales Tax Payable	23,665	20,374
Accrued Payroll and Compensated Absences	90,959	84,601
Deferred Revenue	2,400	2,400
Consumer Deposits	61,023	63,028
Total Current Liabilities	1,196,305	1,323,303
Noncurrent Liabilities		
Deferred Revenue	39,600	42,000
Note Payable	1,000,000	3,000,000
Total Noncurrent Liabilities	1,039,600	3,042,000
Total Liabilities	2,235,905	4,365,303
NET ASSETS		
Net Assets		
Invested in Capital Assets, Net of Related Debt	2,864,152	1,563,215
Unrestricted	5,157,638	6,664,664
Total Net Assets	\$ 8,021,790	\$ 8,227,879

See Accompanying Notes to Financial Statements

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	2011	2010
Operating Revenues:		
Cable System Revenue	\$ 2,082,052	\$ 1,763,505
Telephone System Revenue	1,985,379	2,291,717
Data Services Revenue	1,434,109	1,352,263
Miscellaneous Income	14,928	12,797
	<hr/>	<hr/>
Total Operating Revenues	5,516,468	5,420,282
Operating Expenses:		
Plant Specific and Programming	3,464,441	3,774,548
Depreciation and Amortization	1,159,384	1,150,833
Customer Services and Marketing	580,472	480,457
General and Administrative	593,607	657,110
	<hr/>	<hr/>
Total Operating Expenses	5,797,904	6,062,948
Operating (Loss)	(281,436)	(642,666)
Non-Operating Income (Expense):		
Leased Facilities	178,775	188,116
Net Income from Joint Ventures	65,584	85,931
Economic Development Payment	(37,401)	(27,594)
Interest Income	25,335	21,575
Interest Expense	(141,788)	(137,800)
Inventory Sales	1,012	5,101
Gain on Plant Retirements	-	808
Payment in Lieu of Property Taxes	(16,170)	(640,268)
	<hr/>	<hr/>
Total Non-Operating Income (Expense)	75,347	(504,131)
Changes in Net Assets	(206,089)	(1,146,797)
Net Assets at Beginning of Year	<hr/> 8,227,879	<hr/> 9,374,676
Net Assets at End of Year	<hr/> \$ 8,021,790	<hr/> \$ 8,227,879

See Accompanying Notes to Financial Statements

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
Cash Flows From Operating Activities:		
Cash Received From Customers	\$ 5,352,055	\$ 7,313,891
Cash Payments to Suppliers for Goods and Services	(3,304,695)	(3,280,544)
Cash Payments to Employees for Services	(1,534,553)	(1,431,831)
Cash Payments for Economic Development and In Lieu of Property Taxes	(53,571)	(667,862)
Payments Received From Leasing of Facilities	178,775	188,116
	<hr/>	<hr/>
Net Cash Provided By Operating Activities	638,011	2,121,770
	<hr/>	<hr/>
Cash Flows From Capital and Related Financing Activities:		
Acquisition & Construction of Property and Equipment	(455,525)	(458,842)
Proceeds from Sale of Capital Assets	-	1,100
Note Payable Principal Payment	(2,000,000)	-
Payments Received From Sale of Inventory	1,012	5,101
Interest Paid	(141,788)	(137,800)
	<hr/>	<hr/>
Net Cash (Used) By Capital and Related Financing Activities	(2,596,301)	(590,441)
	<hr/>	<hr/>
Cash Flows From Investing Activities:		
Other Investments	989	82,290
Interest Received From Investments	25,335	21,575
	<hr/>	<hr/>
Net Cash Provided By Investing Activities	26,324	103,865
	<hr/>	<hr/>
Net Increase (Decrease) in Cash	(1,931,966)	1,635,194
	<hr/>	<hr/>
Cash and Cash Equivalents at Beginning of Year	5,262,288	3,627,094
	<hr/>	<hr/>
Cash and Cash Equivalents at End of Year	\$ 3,330,322	\$ 5,262,288
	<hr/>	<hr/>

See Accompanying Notes to Financial Statements

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

**Reconciliation of Operating (Loss) to Net
Cash Provided by Operating Activities**

Operating (Loss)	\$	(281,436)	\$	(642,666)
Adjustments to Reconcile Operating (Loss) to Net Cash Provided By Operating Activities				
Depreciation and Amortization		1,159,384		1,150,833
Leased Facilities Income		178,775		188,116
Contributions Paid for Economic Development		(37,401)		(27,594)
Payment in Lieu of Property Taxes		(16,170)		(640,268)
(Increase) Decrease in Operating Assets:				
Consumer Deposits		2,005		(1,104)
Accounts Receivable		(127,017)		1,747,587
Unbilled Usage		(37,001)		149,526
Materials and Supplies Inventory		(10,860)		(10,828)
Prepayments		(62,870)		14,660
Increase (Decrease) in Operating Liabilities:				
Accounts Payable		(134,642)		154,187
Accrued Payroll and Compensated Absences		9,649		40,617
Consumer Deposits		(2,005)		1,104
Deferred Revenue		(2,400)		(2,400)
Total Adjustments		<u>919,447</u>		<u>2,764,436</u>
Net Cash Provided By Operating Activities	\$	638,011	\$	2,121,770

See Accompanying Notes to Financial Statements

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Basis of Accounting

The Municipal Communications Utility of the City of Spencer, Iowa (Communications Utility or Utility) operates as an independent unit of the City of Spencer and is managed, along with the Municipal Electric Utility and the Municipal Water Utility of the City of Spencer, Iowa, by a five member Board of Trustees. The Utility was formed to engage in the development and operation of a broadband communications system and the marketing of related services such as cable television, telephone, high-speed data communications and other communication products. The Utility's rates are set by its governing board.

For financial reporting purposes, the Utility has included all funds. The Utility has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Utility are such that exclusion would cause the Utility's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Utility to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Utility. It was determined that the Utility has no component units.

The Utility is not considered to be a component unit of the City of Spencer for financial statement purposes.

The Utility's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

In reporting the financial activity of its enterprise fund, the Utility applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure.

The Utility distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. The principal operating revenues of the Utility are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Capital Assets and Depreciation

Capital assets are stated at original cost when first devoted to public service. Currently, such costs include labor-related expenditures, such as payroll taxes, pensions, and other fringe benefits and administrative costs for labor related to the construction of new communications facilities. In addition, net interest costs on construction debt are capitalized. Replacements and betterments of capital assets are charged to capital assets. Routine maintenance and repairs are charged to expense as incurred. Depreciation is calculated on the straight-line basis. Current depreciation expense is approximately 8.83% of the original cost of depreciable communication plant in service.

The estimated useful lives used to depreciate assets by class are as follows:

Infrastructure	10-15 years
Buildings and improvements	20 years
Equipment	5-7 years

C. Accounts Receivable

Accounts receivable are stated at the amount the Utility expects to collect from outstanding balances. The Utility provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowed based on its assessment of the current status of individual accounts. Balances that are still outstanding after the Utility has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements.

D. Inventories

Inventories are valued at the lower of cost or market. The average cost method is used for determining the cost of materials and supplies inventory. Inventories are recorded as an expenditure or, if applicable, capitalized when consumed.

E. Unamortized Deferred Costs

Cable television system costs allocated during construction of the system are being amortized using the straight-line method over the expected life of the cable television plant.

F. Net Assets

Net assets represent the difference between assets and liabilities in the financial statements. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used for acquisition, construction or improvement of those assets and increased by unspent debt when there are limitations imposed on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The Utility's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

G. Income Taxes

The Communications Utility is exempt from federal and state income taxes because it is a governmental entity organized under the provisions of Chapter 388 of the Code of Iowa.

H. Revenues and Unbilled Usage

Revenues are based on billing rates, which are applied to customers' consumption of communications services. The Utility records estimated unbilled revenue at the end of accounting periods. Revenues earned, but not yet billed at December 31, 2011 and 2010, totaled \$238,221 and \$201,220, respectively.

I. Estimates

The preparation of the financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

Note 2 - CASH AND CASH EQUIVALENTS

The Utility's deposits in banks at December 31, 2011 and 2010 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Utility is authorized by statute and Board of Trustees' approval to invest public funds in obligations of the United States government, its agencies, and instrumentalities; certificates of deposit and other evidences of deposit at federally insured Iowa depository institutions; and the Iowa Public Agency Investment Trust.

Interest Rate Risk – The Utility's investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days, but the maturities shall be consistent with the needs and use of the Utility.

The Utility considers all highly liquid investments with an original maturity of three months or less to be cash equivalents for purposes of the statement of cash flows.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 3 - CAPITAL ASSETS

Capital assets activity for the year ended December 31, 2011 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 10,342	\$ -	\$ -	\$ 10,342
Total capital assets not being depreciated	10,342	-	-	10,342
Capital assets being depreciated:				
Infrastructure	10,387,166	322,389	-	10,709,555
Buildings and improvements	944,777	2,074	-	946,851
Equipment	1,280,261	238,251	(107,190)	1,411,322
Total capital assets being depreciated	12,612,204	562,714	(107,190)	13,067,728
Less accumulated depreciation	8,059,331	1,154,587	-	9,213,918
Total capital assets being depreciated - net	4,552,873	(591,874)	(107,190)	3,853,810
Capital assets - net	\$4,563,215	\$ (591,874)	\$ (107,190)	\$3,864,152

Capital assets activity for the year ended December 31, 2010 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 10,342	\$ -	\$ -	\$ 10,342
Total capital assets not being depreciated	10,342	-	-	10,342
Capital assets being depreciated:				
Infrastructure	10,168,875	218,291	-	10,387,166
Buildings and improvements	943,600	1,256	-	944,777
Equipment	1,044,998	239,375	(4,112)	1,280,261
Total capital assets being depreciated	12,157,473	458,843	(4,112)	12,612,204
Less accumulated depreciation	6,917,113	1,146,037	(3,819)	8,059,331
Total capital assets being depreciated - net	5,240,360	(687,193)	(293)	4,552,873
Capital assets - net	\$5,250,702	\$ (687,193)	\$ (293)	\$4,563,215

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 4 - TRANSFERS IN LIEU OF PROPERTY TAX

By resolution of the Board of Trustees, voluntary transfers in lieu of property taxes are made to the City of Spencer, Iowa. Funds totaling \$16,170 and \$640,268 were transferred to the City during 2011 and 2010, respectively.

Note 5 - LONG-TERM RECEIVABLES

During December 2003, the Utility entered into an agreement with Northern Iowa Communications Partners, LLC (NICP), an Iowa limited liability company, pursuant to the provisions of Chapter 28E of the Code of Iowa. Under this agreement, the Utility, along with other members of NICP, agrees to pay for the use of a shared switch for routing certain telecommunications traffic at rates adopted by NICP. The Utility will share in profits generated or shortfalls incurred through the 28E agreement due to the method used to determine an annual usage fee paid by NICP to the Utility. An NICP member will be responsible for maintaining the financial records related to the 28E agreement. The amount earned but not received by the Utility in 2011 and 2010 was \$201,893 and \$231,704, respectively. These amounts are recorded as a receivable.

During May 2006, the Utility entered into an agreement with Evertek, Inc., an Iowa Corporation, to create Clay County Communications, LLC as a separate legal entity. Clay County Communications shall function as if it were a limited liability company organized under Iowa Code Chapter 490A. The purpose of this agreement and Clay County Communications is to provide wired and/or wireless communications services in Clay County, Iowa. The Utility and Evertek, Inc. each initially contributed \$400,000. During 2007 the Utility and Evertek, Inc. each made an additional contribution \$150,000. The Utility accounts for the joint venture on the equity method, and has recorded the balance of \$628,021 and \$533,615 as a receivable in 2011 and 2010, respectively.

Note 6 – NOTE PAYABLE

Note payable activity for the year ended December 31, 2011 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Note Payable - Municipal Electric Utility	\$ 3,000,000	\$ -	(\$2,000,000)	\$ 1,000,000	\$ -

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 6 – NOTE PAYABLE (Continued)

Note payable activity for the year ended December 31, 2010 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Note Payable - Municipal Electric Utility	\$ 3,000,000	\$ -	\$ -	\$ 3,000,000	\$ -

The Board of Trustees of the Municipal Electric Utility adopted a resolution on June 14, 1999, pursuant to Section 384.89 City Code of Iowa and Rule 2.5(5) of the rules promulgated by the City Finance Committee, allowing for the advance of funds not to exceed \$8,000,000 to the Municipal Communications Utility to be utilized for the construction and development of the communication system. These funds are to be repaid upon demand and bear a 4.5% per annum interest rate.

Note 7 - LEASES and LONG TERM DEFERRED REVENUE

Spencer Municipal Utilities entered into a 20 year fiber lease agreement with the Iowa Rural Health Telecommunications Program on July 1, 2009. The contract amount for the lease is \$48,000 and is due in full upon construction completion. Construction was completed and \$48,000 was collected in 2009. Spencer Municipal Utilities recognized \$2,400 and \$2,400 in revenue during 2011 and 2010, respectively. In 2011, there was \$2,400 as short term deferred revenue and the remaining \$39,600 as long term revenue. Spencer Municipal Utilities is responsible for maintenance of the fiber.

The Utility leases building space from the Water Utility. The expense from the lease is classified as operating expense. The lease is a monthly lease based on building space utilized and totaled \$2,368 in 2011 and 2010. The payable at December 31, 2011 was \$2,368.

The Utility leases bandwidth, property, and building space from the Electric Utility. The expense from the lease is classified as operating expense. The lease is a 20-year variable lease based on bandwidth and space utilized and totaled \$411,212 and \$411,213 in 2011 and 2010, respectively. The payable at December 31, 2011 and 2010 was \$411,212, and \$411,213, respectively.

Note 8 - RETIREMENT SYSTEM

IPERS

The Utility contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing, multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, PO Box 9117, Des Moines, Iowa, 50306-9117.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 8 - RETIREMENT SYSTEM (Continued)

Plan members were required to contribute 4.50% through June 30, 2011 and 5.38% presently of their annual salary and the Utility was required to contribute 6.95% through June 30, 2011 and 8.07% presently of annual payroll. Contribution requirements are established by State statute. The Utility's contributions to IPERS for the years ended December 31, 2011, 2010 and 2009 were \$73,200, \$60,526 and \$54,942, respectively, equal to the required contributions for the year.

Employees Pension Plan

All full-time employees of the Communications Utility who have completed six months of continuous employment and are 18 years of age are eligible to participate in a 457b Pension Plan administered by Security National Bank. The Utility contributes 8% of the employees' compensation for all employees contributing at least 2% of their salary.

The Communications Utility's contribution to the Money Accumulation Pension Plan for 2011 and 2010 totaled \$74,300 and \$65,080, respectively.

Note 9 – OTHER POST EMPLOYMENT BENEFITS

Plan Description. The Utility operates a single-employer retiree benefit plan which provides medical/prescription drug benefits for retirees and their family.

The medical/prescription drug coverage is provided through a fully-insured plan. Retirees under age 65 pay the same premium for the medical/prescription drug benefit as active employees, which results in an implicit subsidy and an OPEB liability.

Funding Policy. The Utility currently finances the retiree benefit plan on a pay-as-you-go basis.

Annual OPEB Cost and NET OPEB Obligation. The Utility's annual other post-employment benefit (OPEB) cost is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty years.

The following table shows the components of the Utility's annual OPEB for the year, the amount actually contributed to the plan, and changes in the Utility's net OPEB obligation to the plan:

	<u>2011</u>	<u>2010</u>
Annual required contribution	\$ 10,992	\$ 7,178
Interest on net OPEB obligation	761	482
Adjustment to annual required contribution	<u>(756)</u>	<u>(478)</u>
Annual OPEB cost (Expense)	10,997	7,182
Contributions (estimated)	<u>(297)</u>	<u>(197)</u>
Increase in net OPEB obligation	10,700	6,985
Net OPEB obligation – beginning of year	<u>19,024</u>	<u>12,039</u>
Net OPEB obligation – end of year	<u>\$ 29,724</u>	<u>\$ 19,024</u>

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 9 – OTHER POST EMPLOYMENT BENEFITS (Continued)

The Utility's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation were as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2011	\$ 10,997	3%	\$ 29,724
2010	\$ 7,182	3%	\$ 19,024

Funded Status and Funding Progress. The funded status of the plan as of December 31, 2011 was as follows:

	2011	2010
Actuarial accrued liability (AAL)	\$ 45,009	\$ 36,624
Actuarial value of plan assets	-	-
Unfunded actuarial accrued liability (UAAL)	<u>\$ 45,009</u>	<u>\$ 36,624</u>
Covered payroll (active members)	\$1,009,606	\$1,016,541
UAAL as a percentage of covered payroll	4.5%	3.6%

Actuarial Methods and Assumptions. Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point and do not explicitly reflect the potential effect of legal or contractual funding limitation. The actuarial methods and assumptions used include techniques that are designed to reduce the effect of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the December 31, 2011 actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 4% interest discount rate. The projected annual medical trend rate is 10%. The ultimate medical trend rate is 4.5%. The medical trend rate is reduced 0.5% each year until reaching the 4.5% ultimate trend rate.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 9 – OTHER POST EMPLOYMENT BENEFITS (Continued)

Mortality rates are from the RP-2000 Combined Mortality Table projected to 2010 using Scale AA. The salary increase rate was assumed to be 3% per year. The UAAL is being amortized as a level dollar amount on an open basis over 30 years.

Note 10 - RISK MANAGEMENT

The Communications Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Utility assumes liability for any deductible and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Note 11 - RELATED PARTIES

The Electric Utility, Water Utility, and Communications Utility of the City of Spencer, Iowa exchange services in the normal course of business.

Two members of the Board of Trustees hold non-controlling interests in a financial institution where the Utility maintains cash balances.

Additional related party items are included in Notes 5, 6, and 7.

Note 12 – CONTINGENCIES

In the last four years, the Utility has provided Iowa based telephone numbers to callers who are then connected to a conference call. The Utility maintains these are terminated in Iowa and charges long-distance carriers a fee for terminating access services. The Utility then pays a portion of the revenue to other communication providers who supply a portion of the services. Until 2007 the long-distance carriers have paid these charges to the Utility and the Utility has paid the other communication providers. In 2007, Sprint, has filed a lawsuit alleging that the calls are not terminated in Iowa, and that the Utility is not entitled to the terminating access charges that are billed to them. In 2010, the Utility filed a claim against AT&T for unpaid communications access. The Utility has filed counter-claims or claims against Sprint, Verizon, AT&T and Qwest so that the statute of limitations does not run for filing counter claims. The Utility has also suspended its payments to the other providers pending the outcome of the litigation. In September 2010, the Utility settled its lawsuit with Verizon. The allowance account for carrier receivables was reduced in 2010 by approximately \$3,500,000 due to the Verizon settlement and write off of Qwest receivables prior to January 2009. Management's belief that a reasonable estimate of 15% of the gross revenues generated by terminating these long distance calls will be collected.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 13 - COMMITMENTS

Beginning in 2009, the Communications Utility pledged support to the Iowa Great Lakes Corridor of Opportunity at a level of \$25,000 per year for four years. This commitment is subject to annual review by the Utility Board.

Beginning in 2011, the Communications Utility signed an advertising and signage agreement with the Clay County Regional Event Center. The agreement is effective September 1, 2011 and terminates on August 31, 2014. The annual amount due is \$5,950. A portion of the annual cost is split between the Electric and Water Utility. The Communication Utility is responsible for \$2,677.50 of the annual amount due.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
FUNDING PROGRESS FOR THE RETIREE HEALTH PLAN
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2011**

Year Ended December 31,	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2008	12/31/2008	\$ -	\$ 22,881	\$ 22,881	0%	\$ 958,187	2.4%
2009	12/31/2009	\$ -	\$ 28,668	\$ 28,668	0%	\$ 986,933	2.9%
2010	12/31/2010	\$ -	\$ 36,624	\$ 36,624	0%	\$ 1,016,541	3.6%
2011	12/31/2011	\$ -	\$ 45,009	\$ 45,009	0%	\$ 1,009,606	4.5%

See Note 9 to the accompanying Notes to Financial Statements for the plan description, funding policy, annual OPEB Cost and Net OPEB Obligation, and the funded status and funding progress.

SUPPLEMENTAL INFORMATION

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS
AND CHANGES IN NET ASSETS - BUDGET AND ACTUAL (CASH BASIS)
OTHER SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2011**

	Budgeted Amounts		Actual	Final to Actual Variance
	Original	Amended		
Receipts:				
Municipal Electric Utility			\$ 22,523,494	
Municipal Water Utility			1,708,171	
Municipal Communications Utility			5,558,166	
Total Receipts	<u>\$ 26,395,419</u>	<u>\$ 30,589,200</u>	<u>29,789,831</u>	<u>\$ (799,369)</u>
Expenditures:				
Municipal Electric Utility			20,718,708	
Municipal Water Utility			1,832,905	
Municipal Communications Utility			7,490,132	
Total Expenditures	<u>27,672,300</u>	<u>35,451,228</u>	<u>30,041,745</u>	<u>5,409,483</u>
Net Change in Net Assets	(1,276,881)	(1,962,028)	(251,914)	4,610,114
Net Assets at Beginning of Year	<u>19,184,020</u>	<u>19,184,020</u>	<u>19,184,020</u>	<u>-</u>
Net Assets at End of Year	<u><u>\$ 17,907,139</u></u>	<u><u>\$ 17,221,992</u></u>	<u><u>\$ 18,932,106</u></u>	<u><u>\$ 4,610,114</u></u>

See Accompanying Independent Auditors' Report

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGET TO GAAP RECONCILIATION
OTHER SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2011**

	Cash Basis	Accrual Adjustments	Accrual Basis
Receipts:			
Municipal Electric Utility	\$ 22,523,494	\$ (8,630,937)	\$ 13,892,587
Municipal Water Utility	1,708,171	113,047	1,821,218
Municipal Communications Utility	5,558,166	229,008	5,787,174
Total Receipts	<u>29,789,831</u>	<u>(8,288,582)</u>	<u>21,501,249</u>
Expenditures:			
Municipal Electric Utility	20,718,708	(7,059,052)	13,659,656
Municipal Water Utility	1,832,905	(318,842)	1,514,063
Municipal Communications Utility	7,490,132	(1,496,869)	5,993,263
Total Expenditures	<u>30,041,745</u>	<u>(8,874,763)</u>	<u>21,166,982</u>
Net Change in Net Assets	(251,914)	586,181	334,267
Net Assets at Beginning of Year	<u>19,184,020</u>	<u>41,879,387</u>	<u>61,063,407</u>
Net Assets at End of Year	<u>\$ 18,932,106</u>	<u>\$ 42,465,568</u>	<u>\$ 61,397,674</u>

See Accompanying Independent Auditors' Report

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO OTHER SUPPLEMENTARY INFORMATION –
BUDGETARY REPORTING
YEAR ENDED DECEMBER 31, 2011**

In accordance with the Code of Iowa, Spencer Municipal Utilities annually adopts a combined budget on the cash basis for the Municipal Electric Utility, Municipal Water Utility, and Municipal Communications Utility of the City of Spencer, Iowa following required public notice and hearing. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures. Encumbrances are not recognized and appropriations lapse at year-end.

Formal and legal budgetary control is based upon nine major classes of disbursements, known as functions, not by fund. These functions are public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects and business type activities function and are required to be budgeted.



**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER
MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

Board of Trustees
Spencer Municipal Utilities – Municipal Communications Utility
Spencer, Iowa 51301

We have audited the accompanying financial statements of Municipal Water Utility of the City of Spencer, Iowa (Spencer Municipal Utility) as of and for the year ended December 31, 2011, which collectively comprise the Utility's basic financial statements listed in the table of contents, and have issued our report thereon dated April 4, 2012. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Spencer Municipal Utility's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting described in Part II of the accompanying Schedule of Findings and as item II-A-11 to be a significant deficiency in internal control over financial reporting. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Spencer Municipal Utility's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with

those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

Spencer Municipal Utility's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the Spencer Municipal Utility's responses, we did not audit Spencer Municipal Utility's responses, and accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of Spencer Municipal Utility and other parties to whom Spencer Municipal Utility may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Spencer Municipal Utilities during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Spencer, Iowa
April 4, 2012

Williams+Company, P.C.
Certified Public Accountants

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL COMMUNICATIONS UTILITY
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2011**

Part I: Summary of the Independent Auditors' Results:

- (a) An unqualified opinion was issued on the financial statements.
- (b) Significant deficiency in internal control over financial reporting was disclosed by the audit of the financial statements.
- (c) The audit did not disclose any noncompliance, which is material to the financial statements.

Part II: Findings Related to the General Purpose Financial Statements

SIGNIFICANT DEFICIENCY:

II-A-11 Financial Reporting – During the audit, we identified immaterial amounts of depreciation expense, accounts payable, and revenue not initially identified by Spencer Municipal Utility's internal control. These amounts were either not recorded or not properly recorded in Spencer Municipal Utility's financial statements. Adjustments were subsequently made by Spencer Municipal Utility, if applicable, to properly include or reclassify these amounts in the financial statements.

Recommendation – Spencer Municipal Utility should implement procedures to ensure all accounts are properly identified, classified, and included in Spencer Municipal Utility's financial statements.

Response – We will revise our current procedures to ensure the proper amounts are recorded in the financial statements in the future.

Conclusion - Response accepted.

INSTANCES OF NONCOMPLIANCE:

No matters were reported.

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL COMMUNICATIONS UTILITY
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2011**

Part III: Other Findings Related to Required Statutory Reporting

III-A-11 Certified Budget – Disbursements during the year ended December 31, 2011 did not exceed the amounts budgeted in the business type activities function.

III-B-11 Questionable Expenditures – We noted no expenditures that we believe may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

III-C-11 Travel Expenses – No expenditures of Utility's money for travel expenses of spouses of Utility's officials or employees were noted.

III-D-11 Business Transactions – Business transactions between Utility and Utility officials and employees are detailed as follows:

<u>Name, Title and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u>
Tom Howe, Board Member Part owner of H & N Chevrolet	Maintenance & Repairs	\$ 446

(1) The transaction does not appear to represent a conflict of interest since the total transaction was less than \$1,500 during the year, per Chapter 362.5(10) of Code of Iowa.

III-E-11 Bond Coverage – Surety bond coverage of Spencer Municipal Utilities' officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

III-F-11 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.

III-G-11 Revenue Bonds – No revenue bonds/notes were issued to the Utility.

III-H-11 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12(B) and 12(c) of the Code of Iowa and the Utility's investment policy were noted.

III-I-11 Telecommunication Services – No instances of noncompliance with Chapter 388.10 of the Code of Iowa were noted.